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CARIBBEAN BASIN INITIATIVE

HEARINGS
BEFORE THE
SUBCOMMITTEE ON TRADE
OF THE
COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES
NINETY-SEVENTH CONGRESS
SECOND SESSION
ON
THE ADMINISTRATION'S PROPOSED TRADE AND TAX MEASURES AFFECTING THE CARIBBEAN BASIN

MARCH 17, 23, 24, AND 25, 1982

Serial 97-52

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CARIBBEAN BASIN INITIATIVE

WEDNESDAY, MARCH 17, 1982

House of Representatives,
Committee on Ways and Means,
Subcommittee on Trade,
Washington, D.C.

The subcommittee met at 2:10 p.m., pursuant to notice, in room 1100 of the Longworth House Office Building, Hon. Sam M. Gibbons (chairman of the subcommittee) presiding.

[Press release announcing the hearings follows:]

[Press release of Mar. 3, 1982]

The Caribbean Basin Initiative

The Honorable Sam M. Gibbons, (D-Fla.), Chairman of the Subcommittee on Trade of the Committee on Ways and Means, U.S. House of Representatives, today announced public hearings on March 17, 23, 24 and, if necessary, on March 25, on the Administration's Caribbean Basin Initiative (CBI) announced by President Reagan on February 24, 1982.

The hearings will be held Wednesday, March 17, in the main Committee on Ways and Means hearing room, 1100 Longworth House Office Building, beginning at 9:30 a.m. The hearings on March 23 and following days will begin at 9:30 a.m. in a room to be announced later.

Testimony will be received on the CBI as a whole, focusing particularly on the proposed trade and tax measures. As a result of the inclusion of tax proposals within the scope of this hearing, the Members of the full Committee on Ways and Means will also be invited to attend. If markup sessions are subsequently scheduled on the proposed legislation, the trade aspects of the proposals will be considered by the Subcommittee, whereas the tax issues remain the responsibility of the full Committee.

Administration officials only will testify on Wednesday, March 17. Testimony will be received from the interested public on Tuesday, March 23, Wednesday, March 24, and, if necessary, on Thursday, March 25. Public witnesses will be allotted time for verbal presentations based on the total time available to the Subcommittee following testimony by the Administration. Also, in lieu of personal appearances, any interested person or organization may file a written statement for inclusion in the printed hearing record.

Requests to be heard must be received by telephone to Harriett Lawler by close of business, Wednesday, March 17, 1982. The request should be followed by a formal written request addressed to John J. Salmon, Chief Counsel, Committee on Ways and Means, U.S. House of Representatives, Room 1102 Longworth House Office Building, Washington, D.C. 20515; telephone (202) 225-3627.

In order to assure the most productive use of the limited amount of time available to question hearing witnesses, witnesses scheduled to appear before the Subcommittee are required to submit 75 copies of their prepared statement to the full Committee office, room 1102 Longworth House Office Building, at least 24 hours in advance of their scheduled appearance.

Persons submitting a written statement in lieu of a personal appearance should submit at least six (6) copies of their statement by the close of business Friday, April 2, to John J. Salmon, Chief Counsel, Committee on Ways and Means, U.S. House of Representatives, Washington, D.C. 20515. If those filing written statements for the record of the printed hearing wish to have their statements distributed to the press and the interested public, they may submit 50 additional copies for this purpose if provided to the Committee during the course of the public hearings.

Each statement to be presented to the Subcommittee or any written statement submitted for the record must contain the following information:

1. The name, full address, and capacity in which the witness will appear (as well as a telephone number where he or his designated representative may be reached);
2. A list of any clients or persons, or any organization for whom the witness appears; and
3. A topical outline or summary of the comments and recommendations in the full statement.

Chairman GIBBONS. Good afternoon, ladies and gentlemen. As you know, this is a meeting of the Trade Subcommittee of the Ways and Means Committee, and we are opening hearings today on the President's Caribbean Basin Initiative plan.

We have a very full agenda of administration witnesses this afternoon to discuss the various provisions and implications of the trade and tax portions of the proposed Caribbean Basin Initiative. Since we are covering the tax as well as trade aspects of the initiative, we have invited and welcome the participation of the members of the full Ways and Means Committee and hope that this will be the only hearing on these tax and trade matters that we have to have.

We may not be able to hear all of the administration witnesses today. If we cannot, we will hear some of them tomorrow. The hearing tomorrow morning will begin in this room at 10 a.m. Witnesses from the private sector will be heard next week, on March 23, 24, and, if necessary, the 25th.

We will begin today's hearings with testimony on the one way free trade provisions, which the administration describes as the backbone of its proposed program. Ambassador Brock, with primary policy and coordinating responsibilities as the U.S. Trade Representative, will be our lead witness.

Following his testimony and members' questions, we will have a panel of witnesses from the Departments of State, Agriculture, Commerce, and Interior and the U.S. Customs Service for brief statements, with participation by USTR as well for questions.

We will also have a representative from AID present in case there are any questions about the aid program.

After the witnesses on the trade provisions, we will examine the tax proposals with testimony from the Treasury Department.

Ambassador Brock, we welcome you and it is good to have you appear before the subcommittee again. You may proceed as you wish, with the understanding that your statement and the statement of all other witnesses today will be printed in the record in full.

STATEMENT OF AMBASSADOR WILLIAM E. BROCK, U.S. TRADE REPRESENTATIVE, ACCOMPANIED BY STEPHEN L. LANDE, ASSISTANT USTR FOR BILATERAL AFFAIRS

Ambassador BROCK. Thank you very much, Mr. Chairman.

The President today has transmitted to the Congress the legislation necessary to implement the Caribbean Initiative. This is a multidimensional program combining carefully crafted and focused trade, aid, and investment-related measures. It was designed so these measures would be self reinforcing.

We believe it is comprehensive and addresses both long-term and short-term problems and contains the flexibility needed to respond to the development obstacles of individual countries. It is one element of a broader regional program that can transfer the Caribbean Basin from a region of despair and frustration into a region of peace and freedom. Most important of all, it is a program designed to foster self-reliance.

The President's program for economic revitalization was developed in close consultation with the more than two dozen nations of the Caribbean Basin which are its potential beneficiaries. More than anything else, this program gives expression to the ideas of the people of the region and speaks directly to their aspirations for the future which they will build for themselves.

I believe the title of the act articulates in precise terms the urgent purpose to which the program is directed. The economies of the Caribbean Basin are in critical need of a catalyst that will promote recovery. In the United States today we have become acutely aware of the difficult problems besetting virtually all the world's economies.

The Caribbean, an area of small and fragile economies in the best of times, has been among the hardest hit by recent international economic developments. We are faced in our own hemisphere with a region which is adrift in the world economy and which is nearly defenseless today against the vagaries of the international economy.

As the basin economies have been battered by the oil price hikes and more recently the fall of sugar and other commodity prices, internal tensions have mounted. We now have before us a setting in which violence and political radicalism is flourishing.

The Caribbean Basin Initiative is a response to regional economic problems which must be addressed if this country hopes to live in a hemisphere free from the suffering that is now so vividly apparent in the Caribbean.

The people of the Caribbean are striving today in the same way as are all the people of the Americas to find their place within the evolving world economy of the 1980's. But how can nations such as Barbados or Jamaica achieve this goal in the face of economic obstacles which are posing a serious challenge to nations of many times their size and possessing far greater economic resources.

In the President's message to you he said that our program for the Caribbean was designed to let the people of this region earn their own way. I want to be sure that this committee understands that as far as the people of the Caribbean Basin are concerned, they would not have it any other way. Wherever our delegations went in the Caribbean they talked to people who had confidence in their own future but who felt that in the current environment there existed such substantial impediments to national economic revival that the prospects for totally self-generated recovery were slim.

So they approached us looking for ways in which we might assist them in reducing what we mutually agreed were the most important current obstacles to self renewal. We also agreed that our response to immediate economic impediment should as far as possible be consistent with the goal of long-term development.

Finally, we agreed that there were obligations under the program for all the partners, and actions taken by the United States would be complemented by self-help measures on the part of the beneficiaries.

We can look at some of the impediments which they have identified in consultation with us. The first that I would mention, they were vitally concerned with the question of whether the products of new or expanded production in this region would have liberal access to markets in the United States. While a very high percentage of Caribbean products can now enter our market free of duty under the generalized system of preferences, many potential Caribbean exports have never been included in this scheme.

Other products have been eliminated from eligibility through the GSP petition process or by the competitive need limitations. Although we have been able to maintain eligibility for most Caribbean products, there is uncertainty and fear in the Caribbean Basin about the future of the GSP program.

Further, the Caribbean has not yet been able to use the scheme with the same effectiveness as many other more competitive countries. Accordingly, the President is requesting the authority to grant duty-free access for all Caribbean Basin exports with the exception of textiles and apparels covered by textile agreements, for a period of 12 years.

We think that such an immediate extension of duty-free access on products that have not previously been included in the GSP scheme is warranted and does not pose a threat of injury to any affected U.S. industry. Should, however, a threat of injury or injury itself actually develop, we will retain the ability to safeguard U.S. industry from Caribbean products using the same remedies available under sections 201 to 203 of the Trade Act of 1974.

A second impediment in the view of the Caribbean Basin governments and private sector representatives is the relative unattractiveness of the Caribbean to prospective U.S. investors. Under present circumstances, if a U.S. firm chooses to invest in the Caribbean, it would be disregarding the favorable tax treatment of fixed-asset expenditures which is available in the United States under the domestic investment tax credit.

The simple and, we believe, equitable solution to this problem is our proposal to extend the same type of tax treatment for investments in Caribbean Basin property as is now available for domestic property. This treatment would be extended for a period of 5 years, so in the case of both, our trade and tax proposals, the impact of the measures will depend solely on the initiative of the private sector.

A more amenable climate for commercial activity is being created, but market forces ultimately will determine the success of our joint efforts.

There has been an urgent request by several of the potential beneficiaries for relief in the form of concessional aid. They have sought concessional aid because it is the only practical solution to their very serious balance of payments and debts problems.

The prospects for many of these economically depressed nations would be much worse if there was insufficient credit to support even the most basic private sector borrowing needs. Today the sums that are needed for this purpose are of manageable proportions. The costs that could be incurred from a failure to take remedial action now would be far greater than the provision of these financial resources.

You also have before you certain proposals regarding Puerto Rico and the Virgin Islands. We want to insure that in reducing impediments to economic revitalization in the basin generally, we will be establishing a relationship with Puerto Rico and the Virgin Islands that encourages these islands to play a dynamic role in the region.

One important consideration was the potential effect on their revenues of a duty reduction on rum. Accordingly, we are proposing that all excise taxes on imported rum be rebated to Puerto Rico and the Virgin Islands. Of similar importance will be the granting of tax benefits to these territories, which should eliminate any semblance of fiscal discrimination.

Other steps are proposed, such as the treatment of territorial goods under the trade arrangement rules of origin, which should be of mutual commercial benefit to our territories and to their neighbors in the basin.

What we are seeking in the final analysis is to help the people of the basin build for themselves a better life, not just economically but across the full spectrum of human needs and aspirations. History, and particularly the history of this hemisphere, has demonstrated that a pluralistic society with strong and free private institutions is our best hope in moving toward this ultimate goal.

In administering this economic program we intend to give this institutional aspect particular emphasis by making the granting of beneficiary status dependent upon, among other things, the degree to which workers in each country enjoy reasonable workplace conditions and have the right to associate freely and bargain collectively.

To achieve these goals, we propose to increase by $2 million our foreign assistance spending for the development of free labor movements through the Latin American Regional American Institute for Free Labor Development.

I have spoken today of the serious impediments to renewed economic activity which the basin initiative is intended to address. It represents a mutual commitment to reduce these impediments. Self-help is the final key needed to unlock the door to economic opportunity over the next decade.

Whether we are referring to treatment of new inward investment or the reform of current trade-distorting devices, the nations of the basin must indicate a willingness to direct their economies in a manner conducive to entrepreneurial initiative. As long as the energy and spirit of the private sector is fully engaged, I have confidence that our program will enable the economic revitalization that is intended.

In conclusion, Mr. Chairman, I would simply add my own sense of excitement over this program and my belief that we have developed one that is complementary and each of the parts coherent in the larger context, and one which is important in another sense in that it is a long-term commitment to the economic revitalization and the political pluralism which is an absolute necessity for the long-term success.

I thank you for the chance to be with you today.

Chairman Gibbons. Thank you, Mr. Ambassador, and I want to say I think you have done a good job in helping the President develop this initiative. I know he relied upon you quite heavily. I think it is an innovative initiative. From what little I know of it, I think it is a good initiative.

Perhaps there will be some testimony along the way that will cause me to change my mind, but in the beginning I want to say I support it. I hope I will support it just as vigorously when we come to voting on this legislation, and I hope we can vote on it within a reasonable amount of time.

As you know, Mr. Ambassador, we want to complete the public and private hearings on this before the Easter district work period. The Trade Subcommittee of the Ways and Means Committee will make a tour of the Caribbean Basin, stopping at many of the more important places in the basin during the Easter recess, and perhaps right after that we can come back, deliberate over this matter, and report this bill to the full committee and hopefully get it passed.

So, as far as I am concerned, it is on a reasonably fast track.

Ambassador Brock. We appreciate that very much.

Chairman Gibbons. Now, I want to ask you something about the timetable and the commitments that you expect to carry out under this bill. I note that the bill does not specify when the one-way free trade areas for the Caribbean will go into effect. What do you view the procedure to be and the timetable to be for its implementation?

Ambassador Brock. As soon as we have the authority granted by the Congress, Mr. Chairman, we would again have immediate negotiations and consultations with each of the affected countries. We would hope that that would be a reasonably expeditious process, and once we were assured of the self-help undertakings of those individual nations, the President would designate them and they would from that point forward receive duty-free treatment.

We are talking of a matter of a very short period of time.

Chairman Gibbons. I assume this means you actually negotiate with each individual country in the process and that you will attempt to obtain some kind of prior commitment, at least that they will take certain individual self-help type initiatives of their own. Is that correct?

Ambassador Brock. Precisely.

Chairman Gibbons. Based upon their own individual circumstances. And then there will be some kind of proclamation after that, that that area is then a one-way free trade zone with the exception of textiles and sugar.

Ambassador Brock. That is correct. It would still be one-way free trade for sugar up to the quantity limits.

Chairman Gibbons. Up to some quantitative limits, is that right?

Ambassador Brock. Yes.

Chairman Gibbons. All right.

I assume you have looked at the problem of a GATT waiver. Do you foresee any problems there? Do you know specifically what rules of GATT will have to be waived?

Ambassador Brock. Yes; we have not formally submitted a request for waiver pending an indication of the desires of the Congress, but it clearly would be required, and we frankly do not anticipate any problem with that. A number of countries have sought waivers. If you recall, Australia and New Zealand sought a waiver for some of the island nations in the Pacific. I do not anticipate any problem with that.

Chairman GIBBONS. To date you have not received any specific objections from any of the other GATT countries about that waiver is that correct?

Ambassador BROCK. To my knowledge, that is correct.

Chairman GIBBONS. Fine.

I want to talk next about import relief. This is always a subject that is sensitive to American producers. Will it be more difficult for domestic industries to obtain import relief on imports from the Caribbean than it currently is?

Ambassador BROCK. No, sir. We intend to apply precisely the same safeguards that now exist under current law.

Chairman GIBBONS. What about the other lesser developed countries? Are they seeking this kind of one-way free trade zone with the United States? Are we setting a precedent here that may cause us trouble in dealing with other lesser developed countries?

Ambassador BROCK. We have not had a specific request for identical treatment from any other country as far as I know. I think the question is valid because in fact we are taking a remarkably new step that has not been done before. I would not be surprised if others would not want to be considered.

I think the problems of this region are so close to home and so important that we felt that the decision warranted the degree of action we have taken. I frankly think we can make a case that this is a unique circumstance and that we will have to do that, I am confident.

Chairman GIBBONS. You settled on a 12-year period for this duty-free one-way trade zone. Why did you pick out 12 years?

Ambassador BROCK. I am tempted to respond that we flipped a coin, but it wasn't quite that easy. We looked at a number of different suggestions ranging from 5 to up to as much as 20 years. I think we came to the conclusion that 12 is a realistic period in terms of the normal investment period, that people have to have an assurance well beyond 5. You cannot calculate an investment and require that it be repaid in 5 years when you are going into a new area. We were a little concerned that 20 might limit our flexibility.

As these countries develop, we would hope that they would move back into more of a two-way free trade, Mr. Chairman, and consequently we sort of took the median number of 12.

Chairman GIBBONS. Most of our agricultural products now come from Mexico. There is no fast track provision for getting import relief for these products from Mexico. Why is it necessary to give fast track relief to imported products from the Caribbean areas?

Ambassador BROCK. I think a number of expressions of concern from some of our agricultural interest led us to conclude that the Secretary should be authorized to act very expeditiously in the area of perishable goods, and we accepted the recommendations of the Department of Agriculture in this particular area.

Chairman GIBBONS. Mr. Frenzel.

Mr. FRENZEL. Thank you, Mr. Chairman.

Thank you, Ambassador, for your presentation.

The chairman asked you about the 12-year period. I would like to follow that up with a question about the specific tax treatment which extends for only 5 years. Can you tell us why you picked five there and why it differs from the dozen years of the basic initiative?

Ambassador BROCK. Yes; the basic purpose of this program is to create a magnet opportunity for these countries to be able to attract economic development and investment, whether it is on the part of U.S. investors or others. An investor needs to have some insurance as to the long-term market opportunity for his product, and that is why the 12-year figure was chosen.

The tax section really deals with the construction of that investment, the placing of the facility itself, and we thought that we would like to give a very high and very intense shot in the arm for quick development with the 5-year approach.

The 5 years will be subject to review at the end of that period, country by country, with the Congress, but we did not feel we could suggest a longer period nor did we feel it was necessary. It might be that a better approach could evolve after a period of time as they begin to adjust their own tax policies to their own development rate, so we thought the 5 years was frankly adequate to draw that investment in, in the first place.

Once the investment is there, they needed a longer term for market access.

Mr. FRENZEL. What are you really talking about? They are just making ACRS available to them for 5 years?

Ambassador BROCK. No, sir. We are talking about the 10-percent tax credit, not ACRS.

Mr. FRENZEL. Thank you very much.

Chairman GIBBONS. Mr. Bailey.

Mr. BAILEY. Thank you, Mr. Chairman.

Mr. Ambassador, at one point I think I had an opportunity to tell you some of my doubts and fears. I have got to tell you very honestly that I have them now, and as I, at least, have studied this issue, it is growing. I understand the foreign policy problems, and as I had spoken with you earlier, one of the greatest problems we have, of course, is the American perception of policy and I think, you are very sensitive to that. That limits the vehicles, I think, and it also creates areas of justice.

When we talk about, for example, what kind of energy we put into enforcing countervailing duty statutes, antidumping efforts, what subsidization means, how we utilize investment tax credits in our domestic tax structure, what tariff and nontariff barriers, market entry problems, et cetera, are, for this country, for American workers, for trade readjustment assistance that we fight so hard to provide, training help, attacking structural unemployment problems, all of that context comes together.

We have got a foreign policy problem in the Caribbean, and I happen to share, believe me, very deeply the fears of problems in that area and what they mean to overall American strategic interest.

Now, let's look at our policies here at home and what we are trying to do with this initiative and look at what it accomplishes. Let me tell you why I don't know if it is the best or the honest, or certainly I don't think it can be the advantage-prone way of going after this problem.

If we are going to have this duty-free import zone on certain products, et cetera, what is the nature of the barriers that we are up against down there? I have been doing a little research. Costa Rica and ad valorem—and correct me if I am wrong because I don't have your resources —we have an ad valorem when we get down to the bottom line of 85 percent on a duty range on, for example, take footwear, something that impacts my home State of Pennsylvania. There is a 30-percent import surcharge, 20-percent consumption charge, 10-percent documentation tax, 25-percent import restriction tax.

What do we do for comparative advantage if we are supposed to stand for fair trade or free trade when we provide a tax-free or duty-free import environment for products made for somebody else? In fact, down in Surinam—Embassy notes in a 1979 report that there may be a total ban on imports in 1981.

How do I go to an American worker who is losing a job and justify what is nothing more than the export of technology in a minor sense but at the very least the export of capital via this mechanism? That is all that it is. You know that it is, I know that it is. That is what is involved here. It is a mechanism providing for the transfer of wealth in lieu of other forms of foreign aid and/or assistance.

In light of what this Government's policies have been, don't you think it is hypocritical? How do I explain that to people back home who talk about a bear being loose on the floor of the House?

Mr. Ambassador, you are smiling. I know why you are smiling. I am, too. It is going to be a grizzly bear.

Ambassador **Brock**. I am looking at one of the bears, that is all. [Laughter.]

Mr. **Bailey**. Could you in that context explain how I justify in terms of what we tell American workers and American businessmen, talking about the impact on small business? The President is a sincere, well-meaning man, but how do I explain those things to people back home? How do I explain to a Member of Congress who isn't on the Trade Subcommittee, Mr. Ambassador? How do I do that?

Ambassador **Brock**. First of all, there are some points that I think at least for me justify this effort, and I won't talk about the foreign policy aspect, I am just going to talk about economic policy. First of all, I can't think of a country or product that they produce that has cost us jobs in this country. They produce less than 2 percent of our imports in any product category, so they are not big enough to really cause a problem.

Mr. **Bailey**. You don't include Mexico in that?

Ambassador **Brock**. No, sir, they are not in this.

Mr. **Bailey**. I noticed they weren't. OK.

Ambassador **Brock**. Second—and I think of real consequence—if we are going to for foreign policy reasons, and because we fundamentally ought to be helping people to achieve their freedom, whether it is good foreign policy or not, but if we are going to do that, the old way of going down with a bucket of money really just didn't work that well, in part because the other ingredients were not there, and frankly, we were trying to do it by ourselves.

I think one of the great things about this program is that the dollar contribution of the United States is minimal compared to that which we hope to achieve in the sum total. They are getting more concessional aid out of Mexico and Venezuela than they are the United States. Canada has doubled its budget. We hope to get a good deal of economic support from Europe and Japan. So it has reduced our burden to take this route.

Last, let me just put it to you in short-, medium-, and long-term implications. If we are going to negotiate with these countries in certain self-help measures, I think it is fair for us to point out that some of the steps they have already taken in precisely the kind of area you mentioned are not logical for their own economic opportunity. It doesn't make sense for them to have a duty on those kinds of products which would enhance their own productivity. So, if they are going to really grow, they are going to have to change some of the practices that have retarded their ability to grow.

Mr. **Bailey**. I have two questions in that connection. No. 1, have you factored in the impact on the United States of America? We are running an unemployment rate in Pennsylvania in excess of 11 percent, and you are asking us to accept more. That is what is going to happen here. Have you factored in the social costs, the unemployment costs, the increased tax costs?

We are talking about, at least in the footwear area alone or some of the leather areas that I have checked on, one-quarter of a million workers in the United States of America. They face a structural unemployment problem if we follow this policy, well over 200,000 at the very least, I assure you. Have we factored in that cost?

Second, have you exacted any kind of quid pro quo from the Caribbean nations who are hoping to be the recipients of this policy in return, for example, Panama? We get in a dozen pair per type of shoe. It doesn't matter which type. It doesn't matter whether they can produce a certain type of shoe. You know, there is a lot of range of products here now. One dozen pair per type of shoe; that is, one dozen children's shoes of textile. This is a quota for export. One dozen women's shoes of plastic per year. Have we negotiated or are we going to negotiate in the interest of comparative advantage in productivity in those things that we are trying to foster worldwide?

Ambassador **Brock**. A lot of the island countries are members of the GATT and do adhere to the trade rules. We are trying to encourage them to join more of the codes. Most of the central American countries do not belong to GATT at all, and there are no ground rules for dealing with that kind of problem. And we clearly do think that it would be in their interest as well as in the interest of the world trading system for them to consider seriously, and hopefully positively, association with the international codes that help to deal with that kind of problem.

But let me come back to the point you made earlier, because it is important to note that in the early days of this program, the employment impact will be clearly positive. They are getting investment and aid funds not only from us but from others for the purpose of developing the economic structure. Now, where are they going to buy that? The logical place is here in the United States. I think they will be coming to us.

Mr. BAILEY. There is a little adjective that I used. I am very sensitive to what you say. There are nasty little realities, political realities, disclocations. I use the adjective "structural" unemployment, a very important adjective.

Ambassador BROCK. I heard.

Mr. BAILEY. Let me end with one last question. I yield back the balance of the time that I have exceeded. [General laughter.]

Thank you, Mr. Chairman. You are very kind. We have some island territories down there. We have the Commonwealth of Puerto Rico; we have the Virgin Islands. How have they been impacted? You know, they have got American labor standards and requirements that they have to meet. In the Virgin Islands—I am checking into it now—I don't know about their cattle hide, their export market. They do raise cattle there, incidentally, and Puerto Rico does, too. Has any work been done on the impact of those areas? We have got some good laws for Puerto Rico, and I realize that.

Ambassador BROCK. We have tried to do that. We have had a very extended series of meetings with Puerto Rican officials running from Governor Omare down through the mayor of San Juan, their technicians. We have consciously sought to take every step that we can take to be sure that in fact Puerto Rico and the Virgin Islands benefit from this program, and that in no way are they disadvantaged.

To the contrary, we think they should be the showplace, because they are associated with this country, and if they are damaged in any fashion, it ill-behooves this country to promote a program that would achieve that consequence. So we have very carefully tried to be sure we have taken the steps to see they are in fact enhanced by this effort, and that they do play a lead role in this development because they are important to us.

Mr. BAILEY. I am still studying it, Mr. Ambassador.

Ambassador BROCK. I appreciate that.

Mr. BAILEY. Thank you, Mr. Chairman.

Chairman GIBBONS. Mr. Schulze?

Mr. SCHULZE. Thank you, Mr. Chairman.

Thank you, Mr. Ambassador. If I were going to formulate a policy for the Caribbean, one of the main facets of that policy, I think, would be an effort to encourage investment. In the last tax bill we created some incentives for investment in our country through accelerated depreciation. I have not seen that extending accelerated depreciation to Americans who invest in the Caribbean Basin is a part of the program. I wonder whether that was considered and rejected, or whether it wasn't considered, because it seems to me to be a rather simple extension.

Ambassador BROCK. We did look at it, as we did at a number of other proposals, relief for tax sharing, for example. The problem we face in the Caribbean is that those countries—Jamaica is a perfect example—have tax forgiveness or tax sparing formulations in their present law, and unless we did something to accommodate that, if U.S. investors went down without any tax provision at all, Jamaica would have been subsidizing the U.S. Treasury. That was not our intent, obviously.

We looked at the range of tax alternatives that we had, and I think, frankly, the Treasury Department came to the conclusion, and the rest of us in the final analysis agreed—we had a lot of discussion and debate on the subject—that the simplest and cleanest and quickest approach would be the 10-percent tax credit. But, we did agree that when we came before the committees that had the greater competence in the area—this committee, of course, and the Finance Committee—that we would welcome your suggestions as to whether or not this is the best way to go.

We wanted to provide Puerto Rico with the assurance that they would not be disadvantaged, so we gave Puerto Rico and the Virgin Islands not only the 10-percent tax credit but ACRS on top of that, and we felt that perhaps we should maintain some such advantage because of the disadvantage of being under other U.S. laws, as mentioned by the Congressman.

Mr. SCHULZE. It seems to me we are building in a little bit of disadvantage for capital investment without ACRS.

Ambassador BROCK. We are trying not to do that, and I hope the 10-percent tax credit is adequate. If there is a better way of doing it, I would welcome the suggestion.

Mr. SCHULZE. I know the foreign aid portion is not an area of your expertise, but will there be subsidized loans involved with that as an incentive to invest or an incentive to create employment?

Ambassador BROCK. The aid component is a straight grant of $350 million. On top of that we have asked Eximbank to make a special effort to provide for credit facilities of the sort that you mentioned. We have also asked and received the active support of VOLPEC to provide additional direct loans and insurance backup to these investments.

Mr. SCHULZE. As you know, Mr. Ambassador, I share some of Mr. Bailey's concerns over the employment situation in our country, and I do have some concerns that we are creating incentives for other countries to export their unemployment to us. I wonder if in formulating the policy—whether we looked at the possibility of creating incentives for the production of products which we may now import from other parts of the world where we have relatively unfavorable trade balances, and thereby create a little more incentive to have those products made in the Caribbean Basin. We would not be creating as much unemployment here but we would be kind of shifting production from one area of the world and create more employment in the Caribbean Basin.

Ambassador BROCK. Yes, we have, and we frankly think that will occur. If it doesn't, the program will be less successful than we had hoped. If I can pick up on your previous point, they are exporting their unemployment to us today, and it is called illegal immigration, and it is hard to deal with.

Mr. SCHULZE. That is true, and that is one of the reasons why I commend you for the Caribbean Initiative. I think something has to be done.

Ambassador Brock. Yes; it does.

Mr. Schulze. I realize that is very difficult, but if we could create more specific incentives in more specific areas, so that there would be a lessened impact on the employment level in this country, and shift it to perhaps some other part of the world whose growth rate is higher——

Ambassador Brock. I think that is a fair comment, and we will try to take that into account with our encouragement of their development.

Mr. Schulze. Thank you, Mr. Ambassador.

Thank you, Mr. Chairman.

Mr. Hance. Mr. Ambassador, the sugar industry constitutes probably the single most export item in that Caribbean area, and as I understand, the President's proposal provides for an increase in the volume of duty-free sugar import of some 1.5 million metric tons primarily from the Dominican Republic, Panama, and Guatemala.

Last year we adopted a sugar provision in the farm bill to try to help the domestic sugar industry, which was really depressed at that time, and it is my understanding that the flood of duty-free sugar that came in in anticipation of that legislation really depressed the price. It looks like the Commodity Credit Corp. may end up owning a lot of sugar as a result of the impact of the imports.

My question is, can you assure us that the proposal that we have before us today will not further hamper the administration of the sugar program, and will not undercut the new price support program that we passed, which would in effect threaten the welfare of an industry that is already in trouble?

Ambassador Brock. Congressman, I assure you we have tried to evolve a program that will have the consequence that you prefer. I think you might ask the Department of Agriculture to be more specific in their response from the technical side, but we have very strong representations from Secretary Block and his entire team insisting that this program be carefully, carefully structured and considered so as to not create a new problem.

We tried to do that by putting a 110-percent limit on their shipment over the last 3 years, the high shipment, and by treating the other countries as they are presently being treated under the GSP approach.

Mr. Hance. Do you think this is something that Mr. Smith with the Department of Agriculture would be more inclined to address when he testifies?

Ambassador Brock. We are both prepared to address it. Perhaps he may have more technical responses in terms of the quantities involved, but they were very much involved in the development of the program, and we tried very hard to accommodate their concerns and the concerns that you have expressed today.

Mr. Hance. Thank you.

Chairman Gibbons. Mr. Pease?

Mr. Pease. Thank you, Mr. Chairman.

Mr. Ambassador, welcome. I wonder if I might pursue for a minute the line of questioning raised by Mr. Bailey. This program is designed to be of relatively minimal cost to the United States, or at least to the U.S. Government, and I believe it was Mr. Bailey who pointed out that to the extent that industry would move from Pennsylvania and Ohio down to some Caribbean country, there would be lost revenue and lost income taxes paid and greater unemployment insurance and so on. Has any effort been made at all to calculate the overall public and private impact of this program?

Ambassador **Brock**. Yes, it is extremely difficult. I had several conversations, our staff did, and so did others, with a number of the leaders of organized labor, who expressed the concern, particularly with the possibility of plants leaving and moving down. We have tried very consciously to be sure that nothing in the legislation would encourage that or would support it in any fashion whatsoever.

We are trying to create a circumstance which would create a magnet for new investment, net additional, not for transferred investment. That was not our intention and it would not be appropriate for the U.S. Government to play that kind of role if it were there. So we are conscious of the problem and trying very hard to avoid it. If you want to try to strengthen the legislation to be sure we have achieved our goal, we would welcome your suggestions.

In terms of the overall economic impact, it is awfully hard to quantify what might happen. I think in terms of existing trade levels, the trade figures we came up with—the estimates ran between $500 million and $1 billion of trade. If you rounded off the group, you would probably come around to 800 million dollars' worth of trade opportunity. But, what will be the case 4 or 5 years from now, I think, is the larger question, and we don't know how to answer that. We hope it will be large. Otherwise the program will not have succeeded.

Mr. **Pease**. Would not the extension of the investment tax credit to capital investment in the Caribbean serve on one hand as a magnet and on the other hand as an incentive for industry to leave Ohio and Pennsylvania and go down to the Caribbean?

Ambassador **Brock**. I don't think so. I think there is an awful lot of investment money that is not being invested in this country right now because of our economic circumstance, and because of the fear of inflation and deficit or whatever. But once we turn our economy around, there is the real potential for a substantially improved investment climate here.

If you look at the fact that a company has made the investment, if they have a plant here, and they are not just getting the investment tax credit, they are getting ACRS and a lot of other advantages, there just is no logic to moving that facility, and we would consciously try to discourage that with the application of the policy.

Mr. **Pease**. Let me try to clarify what I am talking about. I just finished talking with 30 industrialists from my area individually over the last 5 weeks, and the medium-sized plants make the point that they want to remain medium-sized, and that if they plan expansion in the next 4 or 5 years, which many of them are, it will not be probably in the same physical site that they are in now. They want to keep their employment around 400 or 500 people. So that means if they have plans for expansion over the next 4 or 5 years, they are looking for another site, and it could be 30 miles from my district or it could be 100 miles or in the next State.

Under those circumstances, it seems to me that an industry that is planning to establish a new plant with 200 or 300 employees adds up the advantages of locating that plant in Ohio or Pennsylvania or Jamaica or some place else. Obviously, one of the things on the side of moving into the Caribbean is lower wages. One thing on the side of keeping it here is the higher skill level. Certainly one argument for keeping the plants here also would be the availability of the 10-percent investment tax credit, and if we eliminate that, it seems to me that that does encourage U.S. industry to think in terms of building the satellite plants in the Caribbean rather than 50 miles from their home plant or 100 miles from their home plant. Is that not correct?

Ambassador **Brock**. I guess my hope is that we will create an economy sufficient to do both. The problem with any company that wants to add a new facility is that they have to look at a lot of different factors. In my earlier days I did a lot of work in trying to get plants out of Ohio into Tennessee.

Mr. **Pease**. You were pretty successful, too.

Ambassador **Brock**. Well, we tried. We thought our first and most important advantage was the fact that wages were a little bit lower in Tennessee, not a lot, frankly, but a little bit.

It turned out that was not the primary concern of the business people we talked to. They were more concerned about the quality of schools and the kind of city to which they would move. They were concerned about the infrastructure, the availability of fire and police protection and the rate of taxing, at a slightly lower level, but that was very important to them.

I think that in the final determination—the last factor, probably the least consequential factor, was the wage pattern. The fact that they cared most about was the kind of community in which they would live and raise their children because they were going to have to live there.

I think you will find that they would be able to match any kind of competition they want to.

Mr. **Pease**. I grant you, that's your experience. The experience I've had in talking with our industry people who have plants in Ohio and Arkansas and Tennessee and North Carolina did not bear that out. But I may be talking to different people.

One other question, Mr. Ambassador. Which nations will participate in this new initiative, and how would we select those nations?

Ambassador **Brock**. All of the nations of Central America south of Mexico and north of Venezuela and Colombia will be participants. The island countries of the Caribbean, with the exception of Cuba, which is covered under present U.S. law which says that we shall not undertake such initiatives with a Communist country. But no other country is excluded.

Each will be dependent upon their desire to work within the framework of the self-help measures that we have established.

Mr. **Pease**. Does that include Nicaragua?

Ambassador **Brock**. If they seek to join and seek to do so in a constructive fashion, they are not automatically precluded. I think it would be very difficult for us to have any kind of conversation with them as long as they are involved in an internal revolution in another country, obviously.

Mr. **Pease**. Thank you.

Mr. **Schulze**. Will the gentleman yield for one brief question?

Mr. Ambassador, in general how has the reception been from the beneficiary countries? Are they enthusiastic, are they ho-hum? How would you characterize the reaction?

Ambassador **Brock**. It has been uniformly good. They feel very strongly that they have the capacity to develop, but they cannot do it all inside. They need some access opportunity to other markets and cash infusion to provide them with the basic ingredients to start.

Mr. **Schulze**. You feel they will be very cooperative in this entire effort and do things internally that will aid and foster that?

Ambassador **Brock**. I really do. They have been extremely willing to work with us and very helpful.

Mr. **Schulze**. Thank you, Mr. Chairman. I thank the gentleman for yielding.

Chairman **Gibbons**. Mr. Jenkins?

Mr. **Jenkins**. Thank you.

Mr. Ambassador, the record of the safeguard mechanism on which the proposed CBI safeguard measure is based, the escape clause, brings to mind some serious questions regarding its ability to adequately protect some domestic industries from import injury. You may recall the Senate Finance Committee had to intervene and initiate an escape clause proceeding for the nonrubber footwear industry in 1976, after the industry had proved serious injury and yet received no import relief. While relief was granted the second time around, of course, we all know that the President terminated relief for this industry as of June 30 of last year.

The question I have is, what makes the administration believe that the safeguards measures proposed now are any more meaningful for import-sensitive industries such as the footwear industry? I understand that you did not include footwear with textiles and apparel.

Ambassador **Brock**. That is correct. Frankly, if we began listing a whole series of industries that would be excluded, the virtue of the program would be lost. We do believe that the present law is adequate if used, and there is every intention on the part of the administration and on the part of industry I think to be sure that in fact the law was used as it was intended.

Mr. **Jenkins**. You do not see any problem in this particular industry from this legislation?

Ambassador **Brock**. If a problem occurs, I think the law is adequate to insure that they will be treated expeditiously and fairly.

Mr. **Jenkins**. I am assuming the reason you did not include leather products or footwear products was because you did not want to get into the situation of excluding an entire list of products; is that right?

Ambassador **Brock**. It is very hard to stop once you start putting names on the list. Textiles and apparel are covered by a multinational agreement. It is well in place and has been for several years. And that's a different category. But that just did not apply in any other circumstance, and we felt that beginning to open the door by just adding individual product items to the list could be destructive of the entire program.

Mr. **Jenkins**. Well, I do have some concerns about it, and I appreciate the fact that you have listed apparel and textiles. When I look at the import figures in those areas over the last 6 or 8 months, it is unbelievable as far as the increase.

Last week I had a plant close with 800 employees. I do not know, very honestly, where we are going to place these people. I do not think there is anyplace to place them now. And certainly all of my textile and apparel, as well as the shoe industry, are pleading daily as they see this gradual increase in those items. And if the figures they are providing me are accurate, we are going to have some long-term problems, or else we are going to lose the industry.

Ambassador **Brock**. I may say on behalf of the industry that, particularly in the shoe industry and in the mill sector of the textile industry, the commitment of those groups to modernization, improved productivity, improved customer service and style work, has been absolutely fantastic, and they have made really incredible progress as a consequence.

They used the time they were given by the agreement very effectively, and it is my belief that by and large they can compete. The problem that most of them has is—and I am setting aside apparel for the moment because that is a very different problem—but most of the difficulties that are faced in these industries are faced by all companies in this country today—automobiles, steel, you name it—and that is the domestic economic circumstance which has so depressed our overall market circumstance.

Mr. **Bailey**. Would the gentleman yield?

Mr. Ambassador, before Mr. Jenkins asked you, Mr. Jenkins had asked about footwear. There are absolutely no leather products of any type, then, that you have included?

Ambassador **Brock**. No.

Mr. **Bailey**. OK. You know, you are talking about an unemployment of better than 210,000 people. No matter how much you modernize and whatever, it has been done, that is labor intensive in many ways. You do have significant import penetration already. If you do not like that terminology, I can understand it, but you would have a significant share already.

Ambassador **Brock**. Yes, we do.

Mr. **Bailey**. I thank the gentleman for yielding.

Mr. **Jenkins**. Well, I will end my questions, Mr. Ambassador. What concerns me even going back to 1980, leather apparel received a unanimous finding of injury under the escape clause in 1980 and President Carter at that time refused to provide import relief. Footwear was turned down by President Ford in 1976.

And frankly, I think the industry thought it had a commitment at that time. Congress then asked that ITC reopen the case and this led to the President, then Carter, providing some import relief. But last June, of course, President Reagan refused to extend the import relief.

I do not know that the leather products industries would have any confidence that the safeguard mechanism will work for them or for any other industry, as far as that is concerned, because the track record is so poor.

Ambassador **Brock**. Well, with all respect, I have to disagree. Whatever the circumstance precedent to this administration, I cannot comment on the cause of their action, but I can say the relief that was granted under the former administration was for a stated period of time. The industry had asked for that stated period of time. They sought it and they got it, and they used it very effectively.

And you know, if you look at the fact that their profit on investment was 28 percent in the year preceding the decision that President Reagan made, that is a more than adequate return on investment, Congressman.

There are some historical reasons. Let me point out to you that when we are talking now about the Caribbean, leather footwear from the Caribbean amounted to less than one-half of 1 percent of our imports of that product, less than two-tenths of 1 percent of our imports of nonrubber, nonleather footwear.

I find it really difficult to believe that that level, one-half of 1 percent or two-tenths of 1 percent, constitutes a real threat to an industry that is just doing a fine job of working its way out of a problem.

Mr. **Jenkins**. Well, I am just trying to protect my industry.

Ambassador **Brock**. I appreciate it.

Mr. **Jenkins**. Thank you, Mr. Ambassador.

Mr. **Bailey**. Mr. Chairman, I would like to inquire.

One more question, Mr. Ambassador. You are familiar with the term "downstream dumping." Allow me to invent a new one or coin a new one. Let us call it "downstream domestic content add-on" or something like that.

Is your structure such that it would discourage a third party from producing a certain portion of a product and sending it to one of these countries for processing and bringing it into the country duty free? I have great strong feelings about the Japanese. I think they are good people, it is a good country. But their business practices I sometimes have to question.

What is going to prevent—not particularly them, of course, but what is going to prevent that kind of practice? Is there anything written in the law that prevents that? I have checked it over and I cannot find where you do.

They have a domestic content now. If you are doing something 65 or 75 percent, whatever, or 25 percent, that has to be their content, what prevents some third party from sending these things down there and adding value to them and coming in here duty free?

Ambassador **Brock**. I think that will happen.

Mr. **Bailey**. That will happen?

Ambassador **Brock**. Yes.

Mr. **Bailey**. I bet it does not.

Ambassador **Brock**. Well, if you look at the law we have presently under GSP, 35 percent value added. We tried to be more liberal in this particular approach and we went to 25 percent value added.

Mr. **Bailey**. It is 25 percent now?

Ambassador **Brock**. Yes. We are going to have to police very carefully to make sure that there is in fact real value added, that it is not simply repackaging, but value added to the actual product.

Mr. **Bailey**. So somebody makes a product which reaches Caribbean country X with 74 percent or 76 percent, rather, of value, of final value or whatever; 24 percent is added and it comes into this country duty free under this plan.

Ambassador **Brock**. No, sir, it would not be able to come in under those circumstances. It would have to be in excess of 25 percent. That is the breaking point.

Mr. **Bailey**. So if it was 74 percent and 26 percent, it comes in duty free?

Ambassador **Brock**. That is right. We have the present law, if you recall; 807 allows us to precut goods and send them down——

Mr. **Bailey**. I am familiar with 807. I am on a bill dealing with just that thing. I think we have got to do all kinds of creative things in this area.

I thank you very much, Mr. Ambassador. Thank you, Mr. Chairman.

Chairman **Gibbons**. Mr. Ambassador, we thank you for the job you have done on this program and the fine job you are doing as the President's Trade Representative.

Ambassador **Brock**. Thank you, Mr. Chairman.

Chairman **Gibbons**. Our next witnesses are a panel representing the various Departments of our Government: the Departments of State, Agriculture, Commerce, Interior, the U.S. Customs Service to be recognized for statements. We will also ask if we have enough room at the table for Mr. Stephen Lande to come forward, the Assistant USTR for the Americas, and Mr. Marshall Brown, Deputy Assistant Secretary from AID.

Have we got all of them at the table here? I guess we have. We have got all the chairs full.

Let us see, we will start off with the Department of State, Ambassador Robert J. Ryan. Mr. Ambassador, you may proceed as you wish. We will take all the panel and then we will come back for questions.

STATEMENT OF AMBASSADOR ROBERT J. RYAN, JR., DIRECTOR, OFFICE OF REGIONAL ECONOMIC POLICY, BUREAU OF INTER-AMERICAN AFFAIRS, AND COORDINATOR FOR THE CARIBBEAN BASIN INITIATIVE, DEPARTMENT OF STATE

Ambassador **Ryan**. I will just go through a portion of my statement, Mr. Chairman.

Chairman **Gibbons**. As I said, all the statements will be included in full in the record.

Ambassador **Ryan**. Thank you.

Mr. Chairman, on February 24, when he outlined our strategy for dealing with the problems of the Caribbean Basin, the President said: "Make no mistake: The well-being and security of our neighbors in this region are in our own vital interests."

The President's program, submitted to Congress today, would advance our national interests in the Caribbean Basin in several ways:

By alleviating the root causes of human misery which have stimulated a major and sustained flow of people from the Caribbean Basin into the United States;

By promoting long-term, self-sustaining growth, thus reducing the need for future assistance from the United States and expanding markets for our goods;

By strengthening regional cooperation and the principle of burden sharing through coordination of our contribution with those of Mexico, Canada, Venezuela, Colombia, and with self-help measures by recipient nations;

By enhancing the security of and prospects for democratic political evolution in the area, thus offering a credible alternative to the thesis that economic progress can only be achieved through violent change and the imposition of undemocratic Marxist governments;

Last, by protecting our strategic and economic interests in the area, by promoting the establishment of stable democratic governments friendly to the United States.

Mr. Chairman, Caribbean Basin countries are, as Ambassador Brock indicated, facing a very difficult international environment. Countries there are experiencing a plague of economic disasters: High rates of unemployment in many countries, 20 to 30 percent or more; low or negative growth. El Salvador is in its fourth consecutive year of falling economic activity, just to cite one example. High inflation, 40 to 50 percent, is not unusual. Massive debts and capital flight—the list could just go on and on. In other words, though, conditions which undermine the confidence of people in these countries that they can survive, much less prosper.

We now have an effective international program and a comprehensive U.S. proposal within that program to address this crisis. With the help of the Congress, the United States will be able to act quickly and effectively to help turn it around.

This program, I think, has several unusual features which assure that it will have a major impact on the region:

First, it is part of a collective effort involving other donor countries, both within and outside the region. As you know, we have worked particularly closely with Canada, Mexico, and Venezuela, and this group has now been joined by Colombia. Secretary Haig and Ambassador Brock met this last weekend in New York with their counterparts from these four countries.

Each of these countries is making a very significant contribution to the economic development of the Caribbean Basin area. These efforts are the more impressive because three of the countries are themselves still considered developing nations. My statement in the record, Mr. Chairman, will summarize these very impressive contributions for you.

We have also consulted with others that have programs and interests in the region, such as European nations and Japan. The international financial institutions have of course also been closely involved in the development of our programs. The Inter-American Development Bank is providing its technical and organizational expertise to form a Central American consultative group. The World Bank is already helping to operate a similar group for the Caribbean.

The strength of this multilateral consultative and coordinating network means that our own efforts in the United States will be neither isolated nor duplicative. The impact of such a coordinated program is bound to be far greater than individual isolated efforts.

Second, this program has been developed through careful consultations with both government and private sector leaders in the Caribbean Basin countries. It reflects not only our analysis of their needs, but more importantly their own priorities and assessments.

We have emphasized to the leaders of the Caribbean Basin countries not only our willingness to help them, but also the fact that our assistance can only be effective if they themselves have well-designed development programs.

Third, the U.S. program has been designed as an integrated system of mutually reinforcing measures. The expanded trade opportunities resulting from the free trade area, combined with the tax investment incentive, will be a powerful stimulus to both local and foreign investors to expand the productive base of the basin economies. Similarly, our assistance program has both a short-term emergency and a longer term developmental component.

In conclusion, Mr. Chairman, let me reiterate that our fundamental goal is to help these countries help themselves. In concert with other nations, we are proposing a program that serves our vital interests by promoting the establishment of a region at peace with itself, free from outside threats, able to devote its energy and attention to economic programs and the development of free political institutions.

Thank you very much, Mr. Chairman.

[The prepared statement follows:]

STATEMENT OF AMBASSADOR ROBERT J. RYAN, COORDINATOR FOR THE CARIBBEAN BASIN INITIATIVE, DEPARTMENT OF STATE

Mr. Chairman: On February 24 when he outlined our strategy for dealing with the problems of the Caribbean Basin, the President said:

"Make no mistake: The well-being and security of our neighbors in this region are in our own vital interests."

The President's program, submitted to the Congress today, will advance our national interests in the Caribbean Basin in several ways:

By alleviating the root causes of human misery which have stimulated a major and sustained flow of people from the Caribbean Basin into the United States.

By promoting long-term self-sustaining growth, thus reducing the need for future assistance from the United States and expanding markets for our goods.

By strengthening regional cooperation and the principle of burden sharing through coordination of our contribution with those of Mexico, Canada, Venezuela, Colombia and with self-help measures by recipient nations.

By enhancing the security of and prospects for democratic political evolution in the area, thus offering a credible alternative to the thesis that economic progress can only be achieved through violent change and the imposition of undemocratic Marxist governments.

By protecting our strategic and economic interests in the area by promoting the establishment of stable democratic governments friendly to the United States.

Caribbean Basin countries are, as Ambassador Brock indicated, facing a very difficult international environment. Countries there are experiencing a plague of economic disasters: High rates of unemployment, in many countries 20 to 30 percent or more. Low growth or negative growth—El Salvador is in its fourth consecutive year of falling economic activity. High inflation—40 to 50 percent is not unusual. Massive debts and capital flight—the Costa Rican government has a foreign debt of almost $3 billion which amounts to over $1,000 per capita. In other words, conditions which undermine the confidence of the people in these countries that they can survive, much less prosper.

We now have an effective international program and a comprehensive U.S. proposal within that program to address this crisis. With the Congress' help the U.S. will be able to act quickly and effectively to help turn it around.

This program has several unusual features which assure that it will have a major impact on the region.

First, the U.S. program is part of a collective effort involving other donor countries both within and outside the region. As you know, we have worked particularly closely with Canada, Mexico, and Venezuela, and this group has now been joined by Colombia. Secretary Haig and Ambassador Brock met this last week-end in New York with their counterparts from these four countries. Each of these countries is making a very significant contribution to the economic development of the area. These efforts are impressive, particularly since three of the countries are themselves still considered developing nations.

Canada has already embarked on a five-year expanded program in the area, at a value of over one-half billion dollars. Canadian tariff treatment also currently provides duty-free or preferential access for some 98 percent of all Caribbean Basin imports.

Mexico and Venezuela are providing an assured supply of oil and long-term concessional credits valued at over $700 million per year. In addition, Mexico is providing trade facilities, preferential credit lines and a broad program or bilateral technical cooperation. Venezuela has provided financial support valued at more than $2.5 billion in the last five years, created a special highly concessional fund for the Eastern Caribbean, and established a strong technical assistance program.

In addition to its existing contributions to the Caribbean Development Bank, the Colombian government is initiating a special technical assistance fund of up to $50 million; new credit lines up to $10 million per country; additional financing for balance of payments deficits; new reciprocal credit agreements; a trust fund for the less developed countries of the Eastern Caribbean; improved trade opportunities; and cooperation for transportation.

We have also consulted with others that have programs and interests in the region, such as European nations and Japan. The international financial institutions have of course also been closely involved in the development of our programs. The Inter-American Development Bank is providing its technical and organizational expertise to form a Central American Consultative Group. The World Bank is already helping to operate the Caribbean Group for Cooperation and Economic Development.

The strength of this multilateral consultative and coordinating network means that our own efforts in the U.S. will be neither isolated nor duplicative. Rather, each international donor or institution—while retaining the freedom to evolve its own programs, and implement them in a way consistent with its own political and economic realites—will be able to support the efforts of other donors. The impact of such a coordinated program is bound to be far greater than individual isolated efforts.

Secondly, this program has been developed through careful consultations with both government and private sector leaders in the Caribbean Basin countries. It reflects not only our analysis of their needs, but more importantly their own priorities and assessments of their needs and their capacity to address their problems.

We have emphasized to the leaders of the Caribbean Basin countries not only our willingness to help them but also the fact that our assistance can only be effective if they themselves have well-designed development programs. Many governments and private sector leaders in the region already recognize the need to reform their policies, and are determined to do the difficult things which are necessary to revitalize their economies. There is also an increasing awareness of the importance of providing the conditions under which private institutions can function effectively. Other countries are still in the process of organizing an effective response to the crises they face. Costa Rica, for example, is a country with a strong democratic tradition which in many ways could be a model for the rest of the region if it could resolve its economic problems. We hope that Costa Rica will soon be able to put together an economic stabilization program which will serve as a solid base for further development in a democratic framework.

Thirdly, the U.S. program has been designed as and integrated system of mutually reinforcing measures. The expended trade opportunities resulting from the free trade area, combined with the tax investment incentive, will be a powerful stimulus to both local and foreign investors to expand the productive base of the Basin economies. Our assistance program has both a short-term emergency and a longer-term developmental component. The supplemental request for fiscal 1982 is primarily designed to provide the productive sector in the Basin countries, which is being strangled by the lack of working capital, with a short-term infusion of credit. This is needed to get operations going again and to turn around the crisis of confidence of many local businesses. We also are proposing financing for programs directed at some of the fundamental structural and institutional inadequacies in these countries. Taken together, this program is focused on revitalizing the productive sector in a way which balances both short-term and long-term objectives.

In conclusion, let me reiterate that our fundamental goal is to help these countries help themselves. In concert with other nations, we are proposing a program that serves our vital interests by promoting the establishment of a region at peace with itself, free from outside threats, able to devote its energy and attention to economic programs and the development of free political institutions. The alternative to action by the United States and other concerned nations is a region increasingly unstable, increasingly hostile to the United States, and increasingly attracted by the empty promises of radical groups supported by Cuba.

Chairman GIBBONS. Our next witness is from the Department of Agriculture, Mr. Smith.

STATEMENT OF RICHARD A. SMITH, ADMINISTRATOR, FOREIGN AGRICULTURAL SERVICE, DEPARTMENT OF AGRICULTURE

Mr. SMITH. Thank you, Mr. Chairman.

I have just a few brief comments I would like to make.

Our Department fully supports this initiative. We feel that our concerns have been fully aired through the interagency process, and we feel that the bill that you have fully takes into account these concerns. We also believe that there are several activities that the Department can participate in in the area which we think would be of mutual benefit to the Caribbean Basin area and to our own interests. We see some potential in working in animal and plant disease eradication in the area for example.

Some infrastructure development we think would not only help the area but would be helpful in our market development activities for agricultural products, and we also see many opportunities in agribusiness that we think would be beneficial to both sides.

In the case of sugar, which is a special case, and one that we were quite concerned with because of the legislation that was recently passed by the Congress, we had long discussions and looked into the situation very thoroughly. We think that the provisions that are included in the bill adequately protect the program, and that is the main objective that we had in that exercise—to make sure that the program was protected.

In the case of perishable commodities, which is another item that is extremely sensitive, we believe the provisions for the fast track action under 201 provision will be very helpful in that regard.

And then, finally, I noted concern about meat imports from the area, particularly from Central America. This legislation in no way changes the existing legislation on meat imports. All imports of meat will still be subject to that legislation.

So, in summary, we feel very comfortable with the legislation, and believe that the interests that I have outlined here are well protected. Thank you.

Chairman GIBBONS. Thank you, Mr. Secretary.

Department of Commerce, Mr. Raymond J. Waldmann.

STATEMENT OF RAYMOND J. WALDMANN, ASSISTANT SECRETARY FOR INTERNATIONAL ECONOMIC POLICY, DEPARTMENT OF COMMERCE

Mr. WALDMANN. Thank you, Mr. Chairman. I would like to briefly summarize my statement which is before you and which I will appreciate having placed in the record.

The comprehensive package of trade, aid and investment measures before you is aimed at two problems: the critical short-term economic problem facing the Caribbean countries and the problem of laying a solid foundation for longer term economic growth and development.

The Commerce Department has participated in development of this program and supports it, and will be involved in the implementation of the program. I would like to discuss briefly with you two areas of special concern to the Department, the role of the private sector in this program and the relationship of the Caribbean Basin Initiative to Puerto Rico.

We believe the private sector will play a vital role in helping to insure the growth of productive capacity in the island economies and in the Central American economies, but we realize that this economic revitalization will not occur overnight. Existing industrial capacity in the Caribbean Basin countries is limited. Businessmen must be made aware of the increased opportunities offered by the CBI, and these in turn must be incorporated into businesses' overall plans.

For this reason, we are announcing today the establishment of the Caribbean Basin Trade, Investment and Business Information Center which will be part of the Office of Central America in the International Trade Administration. This center has been charged with responsibility for providing the full range of support services to U.S. businesses wishing to increase their Caribbean trade and investment activities. The center will provide detailed information to interested private sector individuals and groups on the trade, investment, and assistance programs of the CBI.

The center will be responsible for developing information about the Caribbean countries. The center will participate with USTR and State in consultation with the potential beneficiaries of the Caribbean Basin Initiative, and will discuss with them the extent to which their current policies facilitate or impede trade and investment opportunities.

Second, I would like to point out that in the development of this initiative, we have been, as Ambassador Brock said, quite concerned with the impact that the program would have on Puerto Rico and the Virgin Islands. A special effort was made by the Department of Commerce to insure that Puerto Rico's economic development concerns were taken into account in developing this initiative.

I and others in the group before you have served on the White House Task Force on Puerto Rico, and I also chair the task force's economic subgroup. That subgroup met with Puerto Rican officials on many occasions to discuss the initiative and to discuss the Puerto Rican concerns.

The legislation submitted to Congress today is designed to address Puerto Rico's specific concerns in the following ways. Federal excise taxes on all imported rum will be rebated to Puerto Rico and the Virgin Islands. Inputs from Puerto Rico and the Virgin Islands will be considered as indigenous Caribbean inputs for purposes of the free trade area's rules of origin requirements. This, I might add, will perhaps stimulate a twin plan concept in which the Puerto Rican Government officials are quite interested in.

Third, the benefits of the investment tax credit and the accelerated cost recovery system will be extended to eligible countries operating in Puerto Rico and the Virgin Islands. And of particular interest to the Virgin Islands, an increased allowance for duty-free importation of locally produced alcoholic beverages will be established.

I believe that these measures will create clear opportunities for Puerto Rico and the Virgin Islands to participate in the anticipated overall expansion of economic activity in the Caribbean Basin. We expect that both Puerto Rico and the Virgin Islands will take full advantage of their more developed industrial and service economies to engage in production sharing with basin countries, and to provide them with necessary shipping, banking, construction, and other services.

Mr. Chairman, I would just like to conclude by perhaps anticipating a question which was asked of Ambassador Brock about the leather products industry. In 1980, the countries of the Caribbean Basin exported to the United States approximately 10 million dollars' worth of leather handbags, luggage, and flat leather goods. This accounted for only 5½ percent of our total imports of these items in that year. Therefore we do not anticipate that the free trade area will have a significant adverse impact on the U.S. leather industry.

Thank you.

[The prepared statement follows:]

Statement of Raymond J. Waldmann, Assistant Secretary of Commerce for International Economic Policy

Mr. Chairman and members of the subcommittee, it is a pleasure to appear before you today to discuss and support strongly the Administration's Caribbean Basin Initiative (CBI) which President Reagan announced last month. As Ambassador Brock has already indicated, the President's CBI program is designed to help the Caribbean Basin countries create new productive capacity and take better advantage of existing resources. The comprehensive package of trade, investment and aid measures before you is aimed both at addressing the critical short-term economic problems facing these countries and at laying a solid foundation for long-term economic growth and development in the Caribbean.

I would like to discuss briefly two areas of the CBI program which are of special concern to the Department of Commerce: (1) the role of the private sector in the Caribbean Basin Initiative and (2) the relationship of the CBI to Puerto Rico.

THE ROLE OF THE PRIVATE SECTOR IN THE CARIBBEAN BASIN INITIATIVE

The one-way free trade area, investment incentive measures and economic assistance provisions of the CBI program are designed to promote private sector activity in the Caribbean Basin countries. Increased private sector participation in the development of these economies is essential to the success of the CBI. The private sector will play a vital role in helping to ensure the growth of productive capacity, the efficient allocation of resources and the establishment of a firm foundation for long-term economic growth.

We recognize, however, that economic revitalization will not occur overnight. Existing industrial capacity in CB countries is limited. Businessmen must be made aware of the increased opportunities offered by the CBI and these, in turn, must be incorporated into businesses' overall plans. In some cases, adverse economic conditions in Caribbean countries will continue to impede investment and trade flows unless new policies, aimed at facilitating the free flow of resources, are adopted by these countries.

While the President's CBI package offers attractive incentives for businesses to increase their Caribbean-related activities, follow-up steps clearly are needed to ensure that the private sector is able to take full advantage of the measures.

The Administration has already begun work aimed at ensuring the greatest possible private sector participation in the Caribbean Basin Initiative. As part of this work, the Department of Commerce is announcing today the establishment of a Caribbean Basin Trade, Investment and Business Information Center which will be a part of our Office of Central America. This Center has been charged with responsibility for providing a full range of support services to U.S. businesses wishing to increase their Caribbean trade and investment activities.

The Center's activities will be coordinated with the U.S. Commercial Service and the Foreign Commerce Service located in participating Caribbean countries. The Center will provide detailed information to interested private sector individuals and groups on the trade, investment and economic assistance measures of the CBI program. The Center also will be responsible for developing in-depth information banks on Caribbean country trade and investment policies and conditions. These information banks will be used to identify and evaluate key trade and investment opportunities for U.S. Business and major impediments to U.S. businesses seeking to expand their Caribbean Basin activities. The information banks will form the basis for responding to specific business inquiries concerning trade and investment policies and conditions in Caribbean countries and for designing and implementing seminars and other programs to help expand U.S. business involvement in the Basin countries.

In addition, the Commerce Department's Information Center will play a central role in the Administration's efforts to ensure that beneficiary countries take steps to maximize the potential benefits of the CBI program. As President Reagan emphasized in his February 24 speech to the Organization of American States, the CBI program is designed to help our Caribbean neighbors help themselves by creating conditions under which creativity, private enterprise and self-help can flourish.

Most Caribbean countries export only a limited range of products, many of which are already duty-free. Indeed some 70 percent of total Caribbean non-petroleum exports to the United States in 1980 entered duty-free under the U.S. Generalized System of Preferences or as a result of most-favored-nation duty-free status. The CBI's free trade area and investment measures are designed not only to help Caribbean countries expand their productive capacity in existing industries but also to assist them in diversifying their productive base and thus lay the groundwork for more balanced economic growth. The CBI will be successful in encouraging new trade and investment only if the Caribbean countries also take steps on their own to encourage the free flow of economic resources. Title I of the CBI legislation therefore states that in designating beneficiary countries the President will take into account: the degree to which a potential beneficiary is undertaking self-help measures to promote its own economic development; the overall trade policies of the country (including the use of export subsidies and export performance requirements); and other relevant economic conditions.

The Commerce Department will be participating fully with USTR and the State Department in consultations with potential beneficiaries of the CBI. Using our resources and input from our private sector advisors we will be discussing with the Caribbean governments the extent to which their current policies facilitate or impede trade and investment opportunities and the extent to which new self-help measures to promote private sector economic activity are being planned. In order to ensure that these countries are able to take maximum advantage of the CBI measures, we will propose establishing on-going information exchanges and consultations with them aimed at resolving specific problems facing Caribbean countries and U.S. businesses seeking to expand private sector activities.

It is not possible to quantify precisely either the long-term impact of the CBI on Caribbean countries' economies or the CBI's overall impact on the U.S. economy. We firmly believe that the proposed CBI measures, together with the follow-up plans I described, will provide an important stimulus to promote market-oriented policies and increase production. The economies we are aiding are small, currently accounting for only about two and one-half percent of total U.S. non-oil imports. U.S. industry, however, will continue to have access to protection from serious injury, or the threat thereof, resulting from Caribbean shipments to the United States. In addition, given the strong U.S. position in Basin markets, the Caribbean demand for U.S. exports is expected to increase significantly as Caribbean countries develop.

THE IMPACT OF THE CARIBBEAN BASIN INITIATIVE ON PUERTO RICO

As we developed the Caribbean Basin Initiative, a special effort was also made to ensure that Puerto Rico's economic development concerns were taken into account.

This Administration places a high priority on maintaining our special economic relationship with Puerto Rico. We therefore have consulted closely with the Puerto Rican authorities during the past several months to ensure that Puerto Rico also will benefit and prosper from the CBI program.

In April 1981, the interdepartmental White House Task Force on Puerto Rico was created as a vehicle for communication between Puerto Rico and the Administration. I have served as the Commerce Department's representative on this Task Force and chair the Task Force's Economic Subgroup. The Task Force and Subgroup have met with Puerto Rican authorities on many occasions during the past several months in order to discuss Puerto Rico's concerns and proposals regarding our Caribbean initiative. We also have met with the Virgin Islands' authorities in order to discuss the impact of the CBI on their economy. The CBI legislation submitted to Congress is designed to address Puerto Rico's and the Virgin Island's specific concerns in the following ways: Federal excise taxes on all imported rum will be rebated to Puerto Rico and the Virgin Islands; Inputs (value-added) from Puerto Rico and the Virgin Islands will be considered as indigenous Caribbean inputs for purposes of the free trade area's rules of origin requirements; The benefits of the Investment Tax Credit (ITC) and the Accelerated Cost Recovery System (ACRS) will be extended to eligible companies operating in Puerto Rico and the Virgin Islands; and an increased allowance for the duty-free importation of locally produced alcoholic beverages from the Virgin Islands will be established.

These measures, and the anticipated overall expansion in Basin economic activity, create clear opportunities for Puerto Rico and the Virgin Islands. We expect they will take full advantage of their more developed industrial and services infrastructures to engage in production sharing with Basin countries and provide them with the necessary shipping, banking, and construction services.

During the coming months we will continue to consult with Puerto Rico and the Virgin Islands to ensure that their economies benefit from the implementation of the CBI.

The CBI package presents us with a unique opportunity to aid the development efforts of our Central American and Caribbean neighbors. The integrated program of trade, aid and investment measures which the President has submitted to you is designed to help our neighbors help themselves. With our support, these countries will be able to meet the challenge of restoring economic growth and establishing a more prosperous and just society in which all can benefit.

Chairman GIBBONS. Thank you, Mr. Waldmann.

Our next witness is from the Department of the Interior, Mr. Pedro A. Sanjuan.

STATEMENT OF PEDRO A. SANJUAN, ASSISTANT SECRETARY FOR TERRITORIAL AND INTERNATIONAL AFFAIRS, DEPARTMENT OF THE INTERIOR

Mr. SANJUAN. Mr. Chairman and members of the subcommittee, I would like to summarize my statement as well, and maybe provide a couple of parenthetical statements that have occurred to me as I have heard the hearing unfold.

First, let me say that I worked in the Presidential campaign in the transition to help develop policies that would strengthen our neighboring countries in the Caribbean and Central America. I have also been for about 3 years adviser to the president of the Interamerican Development Bank and was able to get a little historical perspective on the neglect of the Caribbean in the past as far as our policies have been concerned. And then I have been for 3½ years director of the Hemispheric Center of the American Enterprise Institute.

It was in that capacity that I brought for the first time—almost the first time—to Washington a fellow named Ed Seaga, who was a businessman from Jamaica who nobody knew or understood, and who had the audacity to run for the highest office in that land against Mr. Manley, who was running the country with strange socialist formulas. Mr. Seaga told us that what he wanted to do was to get that country patterned after the great success of Puerto Rico and the United States, and what he needed was to be able to help himself. I think he is doing so very well.

Thus, I am a very firm supporter of the Caribbean Basin Initiative. One of the territories that, as Assistant Secretary for Territorial and International Affairs, I deal with is the U.S. Virgin Islands. It is situated in the heart of this very important Caribbean Basin. We have found it appropriate to promote the Virgin Islands interest with relation to the Caribbean Basin Initiative in three different and distinct ways.

First, we seek to offset any direct adverse effect that trade and investment incentives may have on investment in the Virgin Islands. Second, we seek to promote economic development of the Virgin Islands through measures aimed primarily at the private sector so that the territory can maintain its role as a model for growth and development in the Caribbean. And third, we seek to make the territory a partner in our efforts to implement our Caribbean policies throughout the region.

Again, parenthetically, let me say that what we and the administration are trying to do with respect to the Virgin Islands and Puerto Rico transcends the very important measures that protect the Virgin Islands and Puerto Rico in the Caribbean Basin Initiative. There are other efforts underway to try to compensate, if compensation will be needed, and to try to promote better private investment and private sector development opportunities in the Caribbean--airport development, tourist development, and industrial development. They are perhaps related to the CBI, but not directly tied into it.

We in the Department of the Interior have been working very closely with the Virgin Islands and within the Federal Government to protect essential Virgin Islands interests. I have met with Ambassador Brock, Governor Luis, Virgin Islands Senators Lawetz and Paiewonsky, as well as individuals and businessmen from the Virgin Islands. I have had continuing discussions with Virgin Islands delegates, Delegate Ron de Lugo here in the House of Representatives, and I have had many meetings with Rich Williams and Rick Neil in the White House.

I cut short my trip to the Pacific Territories in January in order to attend the crucial January 19 trade policy meeting at the White House on the Caribbean Basin Initiative, as it related to the Virgin Islands and Puerto Rico.

I feel confident in saying that the proposals we have been able to work out and those that still remain to be worked out will assure the Virgin Islands active participation and tangible benefits from the Caribbean Basin Initiative. The Virgin Islands is part of the economy of the Caribbean, just like Guam is part of the economy of Asia. The benefit that the Virgin Islands can derive from economic development of the Caribbean is absolutely obvious to me.

Thank you very much.

[The prepared statement follows.]

STATEMENT OF PEDRO A. SANJUAN, ASSISTANT SECRETARY OF THE INTERIOR FOR TERRITORIAL AND INTERNATIONAL AFFAIRS

Mr. Chairman and members of the subcommittee, it is a pleasure to appear before you today to discuss the impact of the President's proposed Caribbean Basin Initiative on the United States territories.

First, let me say that I worked during the Presidential campaign and the transition to help develop policies that would strengthen our neighboring countries in the Caribbean and Central America and enable them better to meet the challenges of economic development within and political and military intrigue from without. Thus I am a firm supporter of the Caribbean initiative.

As Assistant Secretary of the Interior for Territorial and International Affairs, I have the primary responsibility within the Administration to promote and coordinate the interests of the United States territories and the Trust Territory of the Pacific Islands, areas that, like the Caribbean basin, have great strategic importance and serious problems of economic development. One of these territories, the United States Virgin Islands, along with the Commonwealth of Puerto Rico, is situated in the heart of the vitally important Caribbean basin.

On the one hand, our citizens in the Caribbean welcome the attention and stand to gain by an improved economic and political climate in the area. On the other hand, they are at times apprehensive that some of the proposed measures, particularly in the trade and investment sectors, might dilute their own appeal to mainland investors.

We have found it appropriate to promote the Virgin Islands' interests in relation to the Caribbean Basin Initiative in three distinct ways. First, we seek to offset any direct adverse effect that trade and investment incentives may have on investment in the Virgin Islands. Second, we seek to promote economic development of the Virgin Islands through measures aimed primarily at the private sector so that the territory can maintain its role as a model for growth and development in the Caribbean. Third, we seek to make the territory a partner in our efforts to implement our Caribbean policies throughout the region. These measures we are proposing are before you in the draft legislation submitted by the President.

Our first objective is to minimize the possible negative impact of the Caribbean Basin Initiative. This will maintain the advantages that the Virgin Islands and the other United States territories of Guam and American Samoa, as well as the Northern Mariana Islands, now enjoy vis a vis foreign competitors.

We have proposed that the Virgin Islands be given standing to petition for import relief under provisions of the Trade Act of 1974; this will mean that Virgin Islands industries hurt by import concessions, even concessions predating the establishment of the Caribbean free trade area, have access to safeguard procedures permitting the President to restore duty protection. The rum industry is of particularly vital importance to the Virgin Islands, providing over $37 million in fiscal year 1981 in payments of Federally collected excise taxes. We have proposed an additional safeguard for this rum excise tax revenue by providing for payment to the Virgin Islands of United States excise taxes collected on imported rum. This payment will maintain Virgin Islands excise tax revenues at least at 1981 levels and probably more. The government of the Virgin Islands would then have sufficient resources to promote and protect its rum industry.

Our efforts in the trade area are not limited to protecting the territories from inroads by other nations. We have also proposed a liberalization of the rules under which industries may assemble and ship duty free to the United States products of the territories. We will support amendment of headnote 3(a) of the tariff schedules to raise from 50 percent to 70 percent the limit on foreign components as proposed by Delegate Ron de Lugo last year in H.R. 2232. In addition we have proposed an amendment of customs laws permitting tourists returning from United States territories to bring in duty and tax free an additional liter of locally produced liquor in addition to the four liters now permitted by law.

With regard to investment incentives, we are committed to extending to the Virgin Islands the benefits of accelerated depreciation and tax credits to be provided under the Caribbean Basin Initiative.

Our second objective is to assist the Virgin Islands economy in overcoming some existing problems, primarily in infrastructure development and economic regulation, that will permit the private sector to play a lead role in island development. Our most immediate priority is to see that the St. Thomas airport renovation project is rapidly completed, enabling St. Thomas to compete more aggressively with non-United States islands in the area for the tourist dollar. The application of many federal laws and regulations to the territories appears to present obstacles to economic growth. We propose greater flexibility in the application of these rules. We are now working on application of air and water pollution requirements with the objective of permitting exemptions where justified and authorized. We realize that this is an area where we must tread with caution in view of the importance of clean air and water in a tourist island environment. We have discussions underway with the Environmental Protection Agency to consider a strategy for permitting greater flexibility in emission control expenditure while maintaining high levels of air and water quality. We believe that sufficient flexibility in water quality requirements already exists and we are thus pursuing administrative means for avoiding a major effluent treatment expenditure by the Virgin Islands rum industry.

Again, I emphasize that we do not propose to sacrifice water quality.

Access to credit is a perennial problem for private enterprises in the United States territories, and accordingly, is one more item that we will be considering.

Our third objective is to involve Virgin Islanders in implementation of the initiative. This will certainly benefit both the territory and its Caribbean neighbors, particularly the smaller English speaking states of the Eastern Caribbean. We have already announced support for a planning authorization of $150,000 for an Eastern Caribbean Center as part of the College of the Virgin Islands. The Center would provide training and exchange programs geared to the needs of the Eastern Caribbean. We have also involved Virgin Islands officials in planning meetings and conferences, particularly those related to private sector development of the Caribbean, and we intend to expand these activities.

We in the Department of the Interior have been working very closely with the Virgin Islands and within the Federal government to protect the essential Virgin Islands interests. I have met with Ambassador Brock, Governor Luis, Virgin Islands Senators Lawetz and Paiewonski as well as individuals and businessmen from the Virgin Islands. I have had continuing discussions with Virgin Islands Delegate Ron de Lugo, here in the House of Representatives and frequent meetings with Rich Williamson and Rick Neal in the White House. My staff has been working closely with the Virgin Islands task force on the initiative and with the staffs of the United States Trade Representative and Departments of State, Commerce, and Treasury. I cut short my trip to the Pacific territories in January in order to attend the crucial January 19 Trade Policy Committee meeting at the White House on the Caribbean Basin Initiative as it related to Puerto Rico and the Virgin Islands.

I feel confident in saying that the proposals we have been able to work out will assure the Virgin Islands of active participation in and tangible benefits from the Caribbean Basin Initiative.

Thank you.

Chairman GIBBONS. Thank you, Mr. Sanjuan.

Our last witness on this panel is Margaret M. O'Rourke, who is the Director, Office of Trade Operations, of the U.S. Customs Service.

STATEMENT OF MARGARET M. O'ROURKE, DIRECTOR, OFFICE OF TRADE OPERATIONS, U.S. CUSTOMS SERVICE

Ms. O'ROURKE. Thank you, Mr. Chairman.

I am here representing the U.S. Customs Service, and to support the administration's proposed Caribbean Basin Initiative plan as fully as possible with respect to U.S. Customs.

In reviewing the proposed bill, Customs' main area of responsibility and concern involves the administration of origin and value criteria under section 103. The section provides for duty-free treatment of articles imported directly from a beneficiary country into the Customs territory of the United States, if the sum of the cost or value of the materials produced in the beneficiary country or any two or more beneficiary countries is not less than 25 percent of the appraised value of such articles at the time of their entry into the Customs territory of the United States.

Also, it has been noted that for the purposes of this subsection, 103, the term "beneficiary country" includes the Commonwealth of Puerto Rico and the Virgin Islands. In this regard, Puerto Rico is unique under the provisions of this bill, since it is part of the Customs territory of the United States. Therefore, any merchandise entering Puerto Rico from a Caribbean country would have to meet the 25-percent requirements. Also, goods or components of Puerto Rican origin may be shipped to Caribbean Basin beneficiary countries and counted as part of the 25-percent value added provision previously mentioned.

The 50 States are excluded from counting donor materials or components unless, of course, they are substantially transformed in a beneficiary country before being incorporated into the final product. Accordingly, we contemplate the establishment of suitable documentary controls paralleling those used for the generalized system of preferences [GSP] or item 807 of the Tariff Act.

I appreciate this opportunity of appearing before this subcommittee, and welcome any questions you may have.

Chairman GIBBONS. Thank you very much.

Let me ask the panel a general question to begin with. We have had a number of initiatives toward our neighbors to the south. I remember the most recent one that received widespread attention was the Alianza para Progreso, the Alliance for Progress, in the sixties. Why do you think this one will succeed when others have not been spectacular successes—I hate to call them failures. But why do you think this one will succeed?

Mr. RYAN. I think the key thing there, Mr. Chairman, is that this is not just an aid program. Rather it is, as we indicated, an integrated program of trade, investment, and aid measures. I think that is one important difference with earlier initiatives. I think the second thing I would note is it is not just a U.S. initiative, it is multilateral. It involves a lot of other people, a lot of other donors and international institutions.

So I think it is in both those senses more comprehensive and therefore has a much greater chance of success.

Chairman GIBBONS. What has been the reaction of governments and officials and local businessmen in the various Caribbean Basin countries to the specific initiatives that you propose here?

Mr. RYAN. It has been very positive, Mr. Chairman. During the consultations which preceded decisions in the U.S. program, we detected a great deal of enthusiasm for the sorts of things we were thinking about, and the reaction since the President's speech of February 24 has been almost uniformly positive.

The only negative comments that I know about in the region came from Fidel Castro and Michael Manley, and when I heard those negative comments, I felt that we must really be on the right track. [Laughter.]

Chairman GIBBONS. Would you describe for me what the other four donor countries, Canada, Mexico, Venezuela, and Colombia, intend to contribute to this effort and when they intend to contribute it?

Mr. RYAN. They are already contributing a great deal, Mr. Chairman, and all of them are planning to increase their efforts. As I indicated, we met in New York over the weekend with those countries. You can see in the communique from that meeting a lot of effort on their part. If you wish, I could just briefly summarize what each country is doing.

Chairman GIBBONS. I wish you would.

Mr. RYAN. In the case of Canada, they are doubling their assistance both to the Caribbean Islands and to Central America. Canada also has substantial trade preferences which give duty-free or preferential entry to almost 98 percent of the products from the Caribbean Basin.

Chairman GIBBONS. Let me ask you a question about Canada. What kind of effort do they make to the Caribbean Basin now, and did you say that 98 percent of their imports are now duty-free from that area?

Mr. RYAN. Duty free or preferential entry.

Chairman GIBBONS. Do they make any other effort to assist this area?

Mr. RYAN. I think they have made quite substantial efforts. They mentioned their aid program. They have also done a great deal in the last year or so to encourage their own private sector, to work with the private sector in the Caribbean Basin area. I think for a country of Canada's GNP, their effort is quite substantial.

Chairman GIBBONS. All right, sir, thank you.

Mr. RYAN. Did you want me to review some of the others, Mr. Chairman?

Chairman GIBBONS. Please.

Mr. RYAN. In the case of Mexico and Venezuela, they have a quite innovative program already in effect which they plan to continue. They refer to it as an oil facility. It is similar in some ways to our Public Law 480 programs in the sense that it finances the purchase of oil by Caribbean Basin countries. The value of the program per year is now roughly $700 million, which is a substantial amount indeed for developing countries.

In the case of Colombia, which is a somewhat poorer country than either Mexico or Venezuela, their program is basically a new one, but they are just now undertaking a number of measures in the fields of trade credits, and technical assistance in particular.

Chairman GIBBONS. Let me ask you this. I am sure there will be some concern in our private sector about the fact that we seem to be the only country that is offering a one-way duty-free trade zone out of these five donor countries, including us, and that we may be the target for their exports.

Could you speak to that?

Mr. RYAN. Well, as I indicated, I think the Canadian situation will be similar to ours. I don't think you could logically expect the three developing countries among our partners to do quite the same amount, but all of them are planning to extend trade preferences to the Caribbean Basin area.

Mr. LANDE. If I might add to that response.

Chairman GIBBONS. Would you identify yourself?

Mr. LANDE. Steve Lande of the USTR.

Mexico does provide special trade facilities for Central American countries. Specifically, they provide rebates on the duties paid on a large amount of imports from the Caribbean, from the Central American countries, and they indicated to us in New York last week that they were thinking of expanding that program to include the Caribbean Island countries.

Colombia also indicated at that meeting that after they concluded their negotiations with other Latin American trading partners, particularly those in the Indian Pact, that they also would consider granting trade preferences to the Caribbean countries sometime in 1982. We also believe Venezuela will consider options.

I think the point we should emphasize is all of the developing countries do provide certain forms of duty-free preferences. The European Community gives the Caribbean Islands the benefits of the LOMAT Convention. What we are urging is as many countries as possible to first generalize their assistance so one country doesn't just include the Caribbean Islands and another country doesn't just include the Central American countries, but they include both, and second, of course, to continue to expand those preferences.

Chairman GIBBONS. Thank you, Mr. Lande.

Presently Communist countries are ineligible for GSP treatment unless they are members of GATT and the International Monetary Fund and are not controlled by international communism. The President cannot waive these requirements. Under the CBI proposal, however, the President could waive the exclusion of Communist countries.

Can you explain why this change was made here in this particular area?

Mr. RYAN. As you know, Mr. Chairman, Communist countries, and by this we mean Cuba, obviously would be excluded from the benefits of the free trade arrangement. But since the arrangement goes on for a relatively long period of time, we felt that we should not tie the President's hands completely in this way.

Chairman GIBBONS. Well, I think a more innovative policy toward Cuba may pay off. I am not sure I know which one to advocate, but the ones we have used for the last 20 years have been near disasters.

Mr. RYAN. I do not mean to indicate by this any change in our present policy.

Chairman GIBBONS. I understand that. I just hope you will come up with some idea. I don't have any good suggestions to offer.

Mr. CONABLE. I have a series of questions prepared by Mr. Bafalis who cannot be here today, and I would like to submit them for answer by the panel in writing, if possible, for Mr. Bafalis' benefit.

I would like to ask Mr. Sanjuan a question specifically. It seems to me that what we are doing here is pretty much generalizing what has been our policy toward Puerto Rico all along. Of course, Puerto Rico has a different status than the islands and countries surrounding and making up the Caribbean area.

Is it your assessment that we have been successful in the program we have had toward Puerto Rico? I have knowledge that the per capita income is the highest there of any Caribbean country as far as I know. But we do have some disturbing statistics. About 10 percent of the food stamp money is going to Puerto Rico, indicating that there still remains a great deal to be done after years and years of preferential treatment for Puerto Rico as a part of the United States.

So what reason do we have to expect that a Caribbean Basin program, as diffuse as this will have to be in dealing with institutions which are obviously going to be considerably less meshed with our own, will change the infrastructure and the economic stability of the region if, in fact, after years and years we still have a Puerto Rico whose per capita income is far below that of the rest of the United States?

Mr. **SANJUAN**. Well, Congressman, I appreciate the confidence that you feel in asking me the question; however, let me preface my answer by saying in spite of my name, I am not from Puerto Rico nor am I an expert on Puerto Rico. I am with the Department of the Interior.

Mr. **CONABLE**. You are from Interior, are you not?

Mr. **SANJUAN**. We do not have Puerto Rico under our aegis. We have only the Virgin Islands. But nevertheless, let me try to answer the question.

I think the whole process of development of Puerto Rico until the present time has been one of the most startling and dazzling successes of economic development in the 20th century. From an island that had tremendously underdeveloped economic potential, with the whole process of Operation Bootstrap, and with the whole development of the commonwealth concept until the present time, Puerto Rico has made enormous strides.

In the last few years what has happened, I think, in Puerto Rico is that a formula which succeeded amazingly well raised the standard of living in the island to a level that made that formula less effective than it had been in the past, and Puerto Rico is now in the process of searching, and so are we, I think, in the U.S. Government, for solutions of a different nature and at a different level from that in which Puerto Rico found itself, let us say, in 1948 or 1950 or 1952.

The rest of the Caribbean is, by far, not in the same situation as Puerto Rico is today. Jamaica, the Leeward and Windward Islands, Santo Domingo, parts of Central America—the economic development there is nowhere near what it is in Puerto Rico. Puerto Rico is a hesitating success. The others have not reached economic success of that nature yet. Consequently, I do not think there is a comparison that can be made.

I think that to look at Puerto Rican economic development and political development today and feel that there is failure in the future is very pessimistic. I do not think there is. I think there is a period of adjustment, a period of development that has to attend the change from one type of economic development to what is needed for the future, and diversification of a formula that worked very well until the minimum wage reached a certain level and value added industries found that it was better to go elsewhere.

I do not think that Jamaica, Barbados, or the other islands of the Caribbean or parts of Central America are at that stage, and I think a great deal of the formula that worked in Puerto Rico, if you find an analogy, and I think there is, would work very well elsewhere.

Mr. **CONABLE**. I thank you for your answer.

In view of your statement, I wonder if anyone else has anything they would like to say on that particular subject.

Mr. **WALDMANN**. Thank you, Mr. Conable.

I also do not claim expertise on the Puerto Rican economy, but I think we do have to recognize that there are difficulties in the existing relationship of the U.S. mainland to the Puerto Rican economy, and that these are being addressed by the Governments of both Puerto Rico and the United States now.

But that does not take away from the points that Pedro made; namely that Puerto Rico has been a remarkable success; that for 30 years Operation Bootstrap has brought new employment and new jobs to Puerto Rico; and that we can foresee similar but perhaps not identical activities and operations in other Caribbean countries.

I don't know if the model will be exact, but certainly the measures that we are proposing today will have significant impact on the economies of the other countries.

Chairman GIBBONS. Mr. Bailey.

Mr. BAILEY. Thank you very much, Mr. Chairman.

Mr. Waldmann, what are your feelings about the Economic Development Administration? What is the position of the administration on the Economic Development Administration?

Mr. WALDMANN. The Department of Commerce or the Puerto Rican Economic Development Administration?

Mr. BAILEY. What is the position of the Department of Commerce on the Economic Development Administration of the United States of America?

Mr. WALDMANN. Well, we believe that that Administration should be phased out; that the activities which that Administration represents are more appropriately carried out at the local and State levels; that an Administration which I think now covers some 80 percent of the United States within its purview is no longer focusing on the areas of high priority need in this country.

Mr. BAILEY. I have got a lot of jobs in my district and some very capital-intensive industries which found it difficult to finance modernization projects. I just want you to know that.

Do the Caribbean countries have the equivalent of Economic Development Administrations? I am sure they lack the resources, but do you know? It is probably not a fair question.

Mr. WALDMANN. It is a fair question. I just do not happen to know the answer.

Mr. BAILEY. Does anyone know? I do not expect you to. It would be unfair.

Ambassador RYAN. We can check that for you and submit something further later.

[The following was subsequently received:]

The Economic Development Administration is charged with providing certain kinds of assistance (grants for public works, direct business loans or guarantees, and grants for technical assistance and research and development) to certain areas in the United States specifically designated as economically distressed. None of the Caribbean Basin countries have equivalent institutions. Many do have institutions charged with promoting the economic development of their country as a whole, or of sectors within the economy (e.g., agriculture, industry, etc.), but not of particular geographic areas specifically designated as economically distressed.

Mr. BAILEY. We discussed earlier the question of the add-on problem, and I think we were talking about the 25 percent with the 75 percent add-on problem. Was an analysis done on whether or not that would be a problem? I ask that in connection with the second question for Mr. Alberger here, and for that matter for all of you, for Mr. Ryan too.

I understand that one of the things Canada was going to do, or Mexico, or Venezuela were going to get some cheaper oil, is that right? Cheaper petroleum, was that one of the cheaper things they were going to do?

Mr. LANDE. Yes, sir.

Mr. BAILEY. Is there any structural job displacement that you know of in these other countries? Have you addressed those issues? Do you know anything about that? I am taking you in a three-step process here.

We do not know for sure the role or function. We cannot respond to that, how these parent governments in their concept of free enterprise—the EDA I am sure somehow affects or creates a resource, allocation of credit or subsidy of some type. You are smiling, so I assume I am right about that.

That would be your objection, theoretically and in practice. But we do not know how these governments down there function in their relationship role and function of their government with beginning projects. But let us just assume they are a little more liberal than we are—bad word these days—with those policies. And now we go to a cheaper petroleum. And then we do not know, or do we know, if there indeed is any competition in terms of the impact on unemployment in these other donor countries, as the chairman put it, and us?

You take the area of leather goods, for example. We are talking about potentially at its core affecting 200,000 or so jobs, if in fact they all were lost. But we do not know whether or not Canada really is concerned in that, or Venezuela, because I do not know and I am asking, whether or not they produce in that area. In other words, is this a magnanimous gesture on their part or is it something that, like the Japanese, they would like to give us a better market for navel oranges and baseball bats? I do not know if it is a real sacrifice on their part.

And I ask that in the context of the add-on things. There is a Mazda factory down in Puerto Rico or the Virgin Islands, is there not, where they disassemble the cars and bring them in? I mean, would it be possible at all?

I just lost a factory in my area because of some informal agreements that Canada made, and I sent the information to my Chairman here. If you want to do business in my backyard you had better make sure you add enough value here and do enough of your manufacturing in our country.

With this add-on problem, what kinds of things do Canada, Mexico, or Venezuela export to these countries that may be processed and sold here? Are there any of these cases? I do not know. I do not suspect that there are, but I do not know.

Could you respond if we know the answers to those things, because it is great that these countries are willing to do the things they are doing?

I would rather we get, by the way, Mr. Ryan, an agreement with Colombia on some issues concerning drug traffic, to be very honest with you. I wish we could cooperate a little better there, even more than on the Caribbean initiative.

Mr. **Lande**. Let me try to respond.

Mr. **Bailey**. It is tough, because there are too many unknowns in there.

Mr. **Lande**. As far as the general problem of add-on goes, we have had experience with the GSP system which, as Ambassador Brock pointed out, has a 35-percent direct cost of processing requirement. One point I think I should make—and Ms. O'Rourke may want to go in greater detail—is that is harder than it appears. In other words, it is a direct cost of processing. You do not include indirect inputs or profits. Some people estimate that a 25-percent direct cost of processing requirement is about a 50-percent value added requirement.

Second, in the administration of the GSP program this has not been a serious problem that has been brought to our attention as far as the problem of people who produce a raw product, send it through for a so-called pass-through operation in a developing country and bring it into the United States. Again, it may exist, but at least for countries in the Far East where there may be more of a desire to do this because of the location and proximity to Japan, it has not been yet a serious problem.

Mr. **Bailey**. Mr. Alberger, has Japan been approached to help with this program?

Ambassador **Ryan**. Yes, they have.

Mr. **Bailey**. What kind of response are we getting?

Ambassador **Ryan**. The initial response is positive. But we have to continue talks with them. I did, however, personally visit Japan and make an appeal to them to join in this effort.

Mr. **Bailey**. We'll probably be talking continually 5 years from now.

Ambassador **Ryan**. I think we can make it faster.

Mr. **Bailey**. God bless you, I hope you can.

Mr. **Lande**. It is certainly our hope that given the economic advantages that Japan gets from trading with this area—in fact, I think it is the only country that has a trade surplus with this area.

Mr. **Bailey**. Do they have a Sony television installation down there somewhere?

Mr. **Lande**. I do not believe so. I do not think it has been a center for investment by the Japanese.

Mr. **Bailey**. OK. I do not know either.

Mr. **Lande**. They have some investment in Costa Rica, but not much. Nevertheless, I think it is one of the points of our administration, that certainly given the Japanese position on defense and the fact that they put a great reliance on aid, that given the problems that do exist in the Caribbean, which does have an effect on the Western World, that Japan should carry out significant assistance, whether it be through their private sector, through aid, or through trade. And I think we will keep their feet to the fire in this area, although hopefully they will make the decision based on their own analysis of what is the best type of policy to follow.

As far as your general question on the economic area, if I might return to that for the moment, what we hope would happen from this process is that there would not be a net increase of imports into the United States particularly in import-sensitive products. What we hope will happen is that, as a result of the trade preference and as a result of the tax incentives, production which is now taking place in the Far East or which may be destined to take place in the Far East will begin to be transferred to these areas.

If this occurs it actually has a net advantage to the United States, not only in the political and security area but also in the fact that it is more likely to use inputs from the United States. So the basic thrust of the program and the measures that we have tried to come up with is not to encourage new exports into import-sensitive areas, but to encourage these areas literally to attract industries from other regions.

Mr. **BAILEY**. You want them to compete with the Far East on some of these items. Let us take footwear. You want them to compete more effectively, but not with the American market. You do not think they can necessarily compete with the American market on the world market?

Mr. **LANDE**. I would think if we are successful through relationship in improving the competitive position of the Caribbean vis a vis the Far East through our work in the transportation area——

Mr. **BAILEY**. You would expect them really to replace in the American market?

Mr. **LANDE**. I think that is the basic thrust behind the policy in the multi-fiber area and textiles and apparel, and certainly would be——

Mr. **BAILEY**. And the mechanism by which you're going to achieve this goal is a duty-free import into the United States of items of this sort. But you do not think that is going to impact—5 percent was the figure used by Mr. Waldmann—the market share of those countries, as compared to the American percentage of the domestic market?

You just think it is going to replace the Far East, but it is not going to have any impact on the existing American domestic market?

Mr. **LANDE**. Given the past record of these countries and the need for coming up with a program such as we have in mind, I think one would see certain evidence of that by providing a tariff preference of, I believe in footwear it is what, 7 or 8 percent for nonrubber footwear. Together with the investment incentive, that hopefully would be sufficient to have countries begin to, move out of the Far East into this area, where they could use American inputs, than, encourage people to go to the Caribbean.

The problem in the Caribbean is a serious problem in terms of political stability, and to the extent we can get this investment——

Mr. **BAILEY**. Let me respond to that, sir. Mr. Sanjuan obviously has a very sincere concern. I mean, he cares. It comes through. I want to tell you, I share that. Democracy and its principles to me are probably akin to a transcendental faith to me. Believe me, they are.

And you have got to look at these things, though. When you talk about politics, we have an American domestic political climate to consider. And we sit down and look at these macroeconomic problems and we shift nameless, faceless bunches of Americans around to accomplish diplomatic and military goals and objectives, and we sometimes forget what we went through in the past, when divisiveness and those kinds of difficulties arose.

There is a sense of justice that has to mean something here, too. And you know, "Yankee go home" is a problem. I will tell you, if you think that I think it is going to be increased simply by providing an investment or that the face of capitalism is going to be improved in those countries by virtue of this policy here, I do not agree with you. I will be honest with you, I really do not.

It will go and create more and more problems and abuses in the future. First of all, it is an out and out distortion, and it is a hypocritical distortion of the kinds of things we preach about what policy is supposed to be.

I don't know of alternatives and better ways to do it, but I know we have a problem with the backlash of a protectionist nature. It's sitting out there and it's a specter that's growing in strength every day, and in nothing could I be more sensitive than to what was involved in the Jamaican thing. You know that the Germans and a lot of other people worked very, very hard while we stayed away from that situation, much more than we should have, to accomplish the political changes that took place. You are probably knowledgeable about that. There are a lot of things we can do that are different than this, and I don't think it's the wisest way to go, and I have to share that opinion with you.

I thank you, Mr. Chairman.

Chairman GIBBONS. Mr. Smith of the Agriculture Department, Mr. Hance asked a question about sugar, and he thought he got at least a visual response from you. Could you elaborate on that visual response to Mr. Hance's question?

Mr. SMITH. Well, in the case of sugar, the problem that we had centered around the farm legislation which provides a price support for domestically produced sugar, and obviously, to the extent that you move duty-free sugar, there are some problems associated with that.

The solution that we came up with, and we feel that this will enable us to protect the domestic program, is for the countries that are currently receiving GSP treatment in the region, they will continue to receive it. That doesn't change at all. There are three countries that are major sugar exporters in the region that, because of the size of their exports to the United States, are not qualified for GSP. The CBI legislation would provide them with duty-free absolute quotas which have been based on a historical average, and turn out to be about 110 percent of the best 2 of the last 3 years.

This is a fixed quota. They cannot ship any more sugar than that amount into the market. Associated with that will have to be a look at and revision of the Presidential proclamation that is currently in effect which adjusts the fees depending on market conditions. We will have to take a look at the percentage of sugar that we believe will be coming in duty-free, and also make some assumptions on how the duty-free treatment will be shared between the importers and refiners in this country and the exporters. Based on this, there will likely have to be some adjustments in the fee to assure that we don't get price-averaging that would in essence undermine the domestic sugar program.

We feel that, with those adjustments, we will be able to protect the program.

There is also an escape clause that says that if the Secretary believes that the price support program for sugar beets and sugar cane is threatened by the duty free imports under CBI, he can immediately recommend to the President that the duty-free treatment be terminated.

Chairman GIBBONS. Mr. Jenkins?

Mr. JENKINS. Mr. Chairman, I just have one question.

We do not now have a surplus with these countries as far as trade is concerned, do we?

Mr. LANDE. We have a deficit with these countries, but I believe that if you remove oil from that total, we have a surplus with these countries.

Mr. JENKINS. What makes up the major portion of our exports to those countries? Any particular segment of the——

Mr. RYAN. I think it's very diverse. Lots of capital, equipment, machine tools, things like that; consumer goods. We are the major supplier for most of these countries, accounting for typically 25 percent or more of their markets, so they are getting an awful lot of what they import from us across the board.

Mr. JENKINS. And as far as oil is concerned, that comes primarily just from one of the——

Mr. RYAN. Several of the countries have refineries essentially and export the refined products to us. Trinidad, I guess would be the only one that produces oil on its own.

Mr. JENKINS. OK. Thank you, Mr. Chairman.

Chairman GIBBONS. Let me ask a little about textiles, because this is always a worrisome area. What types of textiles are exempt from the duty-free area?

Mr. LANDE. The textiles that are covered by the MFA, the multi-fiber arrangement, are exempt from the duty-free area.

Chairman GIBBONS. Does this mean if any article is under MFA, it's out of the duty-free area?

Mr. LANDE. That's exactly what it means, sir.

Chairman GIBBONS. What about leather wearing apparel?

Mr. LANDE. That is included in the duty-free area because it is not subject to the multi-fiber arrangement. Leather is not subject to the MFA.

Chairman GIBBONS. How will the administration manage to grant more liberal trade to the Caribbean countries under our MFA bilaterals and still meet its commitments to restrict the overall growth in the market?

Mr. LANDE. The Caribbean provides only a very small percentage of imports of textile and apparel. I believe 3 percent. And within the confines of the arrangement, we find the basic commitment to be particularly strict with the growth possibilities in the large Far East suppliers. There is a possibility for increased growth from the Caribbean, consistent with the overall administration policy for the MFA.

Chairman GIBBONS. On the question of multi-fiber arrangement bilaterals, what is the timetable for negotiating with major Caribbean suppliers?

Mr. LANDE. I think I would have to submit that to you in writing. I do know that we are in the process of negotiating with Haiti at the moment. The only two additional countries that we have bilaterals, I believe, that are in effect now are with the Dominican Republic and Costa Rica. I think they come up next year, but I would rather check it and submit that response to you.

Mr. **Waldmann**. I have the information. The Dominican Republic agreement expires in May 1983; and the Costa Rican agreement in December 1983. So Mr. Lande is right, these do run through early next year, at least.

Mr. **Jenkins**. Mr. Chairman, will you yield?

You've raised a question I want to follow. As far as any liberalization in these countries as far as garments and textiles are concerned, you indicated 3 or 4 percent of the marketplace.

Now if I understand your answer correctly, what we will have to do in order to keep the containment on as far as the growth in these areas is to tighten up on the Far Eastern bilaterals. Is that correct?

Mr. **Lande**. That is correct, sir.

Mr. **Jenkins**. Now the point I want to make, are we in fact doing that? We are in the process now in these Far Eastern countries—I don't see any tightening up.

Mr. **Lande**. We do have a team that is in Hong Kong, and I certainly know that it's the thrust of that team's negotiation to be more strict with the larger suppliers such as those in the Far East than in other areas.

Mr. **Jenkins**. I know that's what we want to do, but from the figures I see, we are going the opposite direction over there. We are increasing, we are not decreasing. We are not tightening up. So I don't see any room. I'm perfectly willing and able to agree to the Caribbean increase if in fact there is a restriction in the bilaterals of these other countries, which I don't see.

Mr. **Waldmann**. If I might comment on that, I think what you see is imports under the existing bilateral agreements and not under the agreements which are being negotiated. In Hong Kong, Korea, and Taiwan, agreements are all being negotiated this spring and summer. They do expire this year, and the policy is, as Mr. Lande said, to tighten those agreements.

Mr. **Jenkins**. Good. I hope that we would have those consummated before this legislation has to come up, because I don't want to get out on a limb on this one until I see what you have done—what we have done in the Far East. I've been down that road before, and I'm pleased that they are terminating this year, and I hope that we can see the results of this before we get into this.

Mr. **Lande**. The legislation itself does not provide for any provisions concerning more liberal treatment for the Caribbean, nor for that matter does it cover the question of quotas. Those are carried out within the discretion of the administration, and the textile negotiations.

But again, I can assure you it is the intention of this administration in administering the textile program to take into account both the interest of the Caribbean and the commitments that have been made to the textile and apparel industries.

Mr. **Jenkins**. I'm sure that is the intent. But, if what my people are telling me is happening is correct, then I think we are going in the other direction. As someone indicated, it's probably under existing bilaterals. I just would like to see some containment in the new bilaterals, and I will be very anxious to see those and hopefully we can see that before this legislation comes up.

Chairman GIBBONS. I want to thank the panel, but before I do, let me say, Ms. O'Rourke, we have some questions for you in writing which we would ask you to respond to.

[The questions and answers follow:]

QUESTIONS AND ANSWERS ON RULES OF ORIGIN UNDER CARIBBEAN BASIN INITIATIVES

Question. How will Customs determine whether a particular product imported from a Caribbean Basin country has met the proposed requirements for duty-free entry.

Answer. Section 103 of this bill closely parallels section 504(b) of the 1974 trade Act with respect to the Generalized System of Preferences (GSP) rules of origin. In conjunction with the GSP, the Treasury Department issued Customs Regulations which required that an article be "the growth, product or manufacture of a beneficiary developing country," before it is eligible for GSP benefits. The Administration will recommend to the Treasury Department that a similar requirement be issued for the Free Trade Arrangement (FTA) under the Caribbean Basin Initiatives (CBI). If such a procedure is followed, Customs administration of the FTA will involve essentially the same origin criteria as now utilized under the GSP, with which we have had over 6 years of administrative and enforcement experience. Consequently, while the requirement for direct shipment is relatively easy to enforce, due to the "paper trail" of imports, consisting of purchase orders, confirmations, invoices, bills of lading, insurance, and other documentary evidence, the value added provision represents significant problems which are compounded by the fact that the imported articles do not have to be the growth, product, or manufacture of the beneficiary country or countries. Customs will accordingly have to rely on the exporting countries certification and the importers' declaration, to the effect that to the best of his knowledge, the information provided with the entry is true and correct. In this respect, it is noted, that unlike the Generalized System of Preferences, there is no limitation on preferential treatment under this bill, therefore, the responsibility and advantage providing and ensuring precise, reliable export certification is substantially reduced and further diminished by the provision for donor content from Puerto Rico and the Virgin Islands.

Question. In your testimony you state that you contemplate documentary controls paralleling those used for GSP *or* item 807. When will you make a determination and what are the pros and cons of the two alternative methods?

Answer. It would be premature to say when we will make a determination as to which documentary controls we would use. Federal rule making procedures require that we publish proposed rule changes and allow a period for comments. Until we have a final bill we would not be able to act. The pros and cons are as follows.

PRO. For GSP, the certifying authorities and documentary requirements are already essentially in place.

CON. In questioning any document under GSP, we are sometimes questioning the veracity of the beneficiary government itself.

PRO. The documentation required under item 807.00 of the Tariff Act would be in the form of a manufacturers' declaration together with the importer's declaration that to the best of his knowledge, the information provided with the entry is true and correct. The manufacturer's declaration would state what processing is done in the beneficiary country and how the cost breakdown of processing and components meets the 25 percent requirement. This procedure allows us to call into question the importer of record and the manufacturer.

CON. Many times the documents are self serving and difficult to verify.

Question. What is your assessment of the impact of these rules in terms of: (1) increasing imports in the United States from the Caribbean and (2) the degree they may offset potential economic disadvantages to Puerto Rico and the Virgin Islands under the CBI?

What particular types of products might be affected most by the proposed rules of origin?

Answer. It is anticipated that the impact of any increased CBI imports can be effectively controlled under these rules with the necessary proportionate allocation of resources for administration and enforcement. The designation of Puerto Rico and the Virgin Islands as beneficiary countries under the Act is of substantive economic advantage because of the entitlement of their products to automatic inclusion in the 25 percent value-added requirement.

Question. Is the "substantial transformation" requirement and its administration, of a greater or lesser impact than the level of percentage itself?

Answer. "Substantial transformation" is uniformly applied to all U.S. imports in determining origin. If an imported article meets this test, it may be marked "made in" the country where the transformation takes place.

This requirement is basic and, therefore, its impact would be greater than the value added level of the percentage itself. Further, all U.S. statistical import data is compiled on the basis of country of origin.

Question. Would you explain your requirements that input from a foreign country must be "substantially transformed" into a new or different final product in the beneficiary country in order to be included in the minimum local content? How do you make this determination?

Answer. "Substantial transformation" confers origin upon materials or components. In other words, foreign input in the form of materials or components would have to be transformed into new and different articles of commerce before being incorporated into the final product in order to be counted in the 25 percent value added requirement.

The requirement that the article be a product of the beneficiary country would give the principle of "substantial transformation" prime importance. Products which are merely packaged or subjected to superficial processing would not meet these requirements.

As an example, concentrated orange juice brought into a beneficiary country in drums and then packaged in individual containers for shipment to the U.S., would not be considered substantially transformed.

Chairman GIBBONS. I want to thank all the panel for your courtesy today, and for your preparedness today, and for your role in developing this program. Let me say, we are very concerned about the role of Puerto Rico and of the Virgin Islands, and I am glad that you all have done as much consulting with them as you have.

We plan to look at their problem specifically and how they interact, but I tend to agree, I think, with the thrust of the testimony of this panel, which is that really the development of those islands is greatly dependent upon development of the basin, and that perhaps that is the greatest gain we will get out of all of this.

Thank you very much.

Our next witness is Mr. Bill Alberger, Chairman of the U.S. International Trade Commission.

Chairman GIBBONS. Mr. Alberger, you are no stranger to this room or this committee or this subject, so you may proceed as you wish.

STATEMENT OF BILL ALBERGER, CHAIRMAN, U.S. INTERNATIONAL TRADE COMMISSION, ACCOMPANIED BY WILLIAM HART, DIRECTOR OF EXECUTIVE LIAISON AND TRADE AGREEMENTS AND WILLIAM GEARHART, ASSISTANT GENERAL COUNSEL

Mr. ALBERGER. Thank you, Mr. Chairman, and members of the subcommittee.

I am accompanied today by Bill Hart, our Director of Executive Liaison and Trade Agreements, and Bill Gearhart, an Assistant General Counsel.

I am pleased to have the opportunity to appear before you today to comment on the prospective impact on the U.S. International Trade Commission of the President's proposal for across-the-board duty-free treatment for most imports from certain Caribbean countries as part of the administration's Caribbean Basin Initiative. My comments will be brief.

If the legislation as presently drafted by the administration is passed, we believe there would be relatively little impact in the way of new demands for resources on the International Trade Commission over the next 4 or 5 years. Any significant impact would arise as a result of petitions for import relief under section 201 of the Trade Act of 1974.

We note that prospective beneficiary countries, individually or as a group, have figured as significant suppliers in very few of our investigations under section 201 of the Trade Act of 1974 or its predecessor provision, section 301 of the Trade Expansion Act of 1962.

We think this situation would likely continue at least for the next few years until new industries have had time to develop in those countries to take advantage of duty-free entry into the U.S. market. The very large percentage of imports from CBI countries which already enters the United States free of duty reinforces this opinion.

It would appear likely that any petitions which might be filed specifically with respect to duty-free treatment under the CBI within the next few years could be in the area of perishable agriculture products.

The proposed legislation would require the Commission in all future section 201 investigations to specifically make a determination as to whether imports from CBI countries are causing serious injury, or threat thereof, to a domestic industry, and the extent to which a remedy should be applied to such imports. This, of course, is an additional task in such investigations.

The provisions in section 103(d)(4) appear to be parallel to sections 203(f)(3) and 203(f)(4) of the Trade Act of 1974, dealing with 806.30 and 807.00 and with GSP. However, there may be some uncertainty generally as to the causation standard for analysis of the impact of imports from the Caribbean nations. One could ask whether such imports alone must be a substantial cause of the serious injury or whether they must merely contribute to the injury.

I have one further comment on the possible impact of the CBI on my agency. We note the absence in the administration's draft of provisions requiring advice from the Commission on the possible economic effect on domestic industries of removing current duties on products from prospective CBI beneficiaries.

We note also that, at least for the past few decades, the Congress has not delegated tariff reduction authority to the President without requiring such advice. In the event that Congress includes in the legislation that is finally passed a requirement for such advice, either to the Congress or to the President, we estimate that such an investigation would cost the Commission at least $100,000. This is a very preliminary figure derived partly from the cost of our recent investigation on granting GSP beneficiary status to the People's Republic of China, $87,000, and the advice to the President on the probable economic effect of possible tariff reductions under section 124 of the Trade Act of 1974 which was $210,000.

In closing, I presume we will be asked officially to comment on the legislation which the administration has proposed, at which time we will have a number of technical comments on the bill.

Thank you for the opportunity to address your subcommittee.

Chairman GIBBONS. Are these advices to the President made public?

Mr. ALBERGER. On GSP right now they are not made public until a certain amount of time has passed, at which point USTR is making them public, deleting only business confidential information that we supplied them. That situation may change based on some discussions I have had with officials at USTR.

Any reports we have made to the Congress again are made privately to the Congress, and at the discretion of the committees involved they have been made public in the past.

Chairman GIBBONS. From your previous experience in import relief cases under what types of economic circumstances do you believe it will be possible for your agency to distinguish sources of injury and determine whether a particular remedy should apply to the Caribbean Basin?

Mr. ALBERGER. That would be a difficult process trying to isolate the impact of particular imports. It would depend probably upon the pricing strategies that were employed. If particular countries were pricing at the lowest levels in the United States, it would be clearer perhaps if the volume is significant, those might be leading to price suppression or depression.

It would depend on the circumstances of the case, but I will grant you that is not a very easy process to follow in order to isolate the impact of particular imports. However, we have to do it when we have multiple cases under the anti-dumping and countervailing duty statutes. So we will certainly do the best we could.

Chairman GIBBONS. Do you have any views on the interrelationship or impact of the emergency relief provisions for agricultural perishables administered by the Secretary of Agriculture and the President and the ITC import relief investigations that would occur simultaneously on these products?

Mr. ALBERGER. As I understand the provisions in the legislation, it would allow for emergency action to be taken during the pendency of a Commission investigation or just prior to it. So I do not think that would have any impact on our investigation as such. We would conduct the investigation as we do now. The mere fact that some emergency action had been taken I do not think would have any impact on our investigation. It would, of course, preclude us from looking if we are doing a 6-month investigation at imports during the first 1 or 2 months of the investigation if they have been stopped, but I do not think that is a serious bar to our looking at the circumstances of serious injury and causation.

Chairman GIBBONS. After you have had time to thoroughly examine the legislation, we would certainly appreciate your comments on any portion of it, particularly the technical portions, because we realize you deal with this on a constant basis.

Mr. Bailey.

Mr. BAILEY. Thank you, Mr. Chairman.

Mr. Alberger, I was calling someone else by your name on the former panel.

Mr. ALBERGER. I heard that. I think that was Steve Lande of USTR.

Mr. BAILEY. I apologize. [Laughter.]

He did not seem to mind, though, so you must be well thought of.

I really have a great deal to learn about this area, and I am anxious to do that. I want to pursue a question that the chairman asked about asking your advice.

When was this proposal drafted, do you know?

Mr. ALBERGER. Well, as I understand it, it was a joint effort of many agencies of the executive branch. We had Mr. Hart sitting to my right here of our staff sitting in on the drafting sessions.

Mr. BAILEY. You did have somebody sitting in on the drafting sessions?

Mr. ALBERGER. Yes.

Mr. BAILEY. Mr. Hart, did you make the suggestion that the ITC's advice should be asked on this point? I do not know much about this.

Mr. HART. We participated in this operation in a purely technical sense. We do not get into the policy sense. I did, of course, raise the question as to whether or not they were going to have——

Mr. BAILEY. Is it on the record you raised that question?

Mr. HART. There was no record.

Mr. BAILEY. It is just an informal get-together?

Mr. HART. Yes; but it was a policy of the decision from the beginning that the legislation would not contain a section calling for advice.

Mr. BAILEY. You raised the question, they were aware of it, and it was discussed as a policy matter, and it was not an omission due to negligence or lack of knowledge. It was a specific policy decision not to.

Mr. HART. That is correct.

Mr. BAILEY. Is that right.

Mr. HART. You might say there is some question about the appropriateness of having such an investigation if they are going to put everything on a duty-free list unlike a trade negotiation.

Mr. BAILEY. Play the devil's advocate for me, because you know the area much better than I. I asked that question in all sincerity. What harm does it do?

Mr. HART. It does not do any harm.

Mr. BAILEY. It does not do any harm?

Mr. HART. No; but in the past this has provided an opportunity for the President to pick and choose among the things that he is going to negotiate on. If the decision has been made that they are going to put everything on a duty-free list——

Mr. BAILEY. It seems to be an irrelevancy. You would argue that it's irrelevant.

Mr. HART. Somewhat. Now, that does not mean that such advice is irrelevant in the whole process.

Mr. BAILEY. I would not think it would be irrelevant in the whole process. I know we have got to got out there and save money and I know every penny counts, and I know Uncle Sam is just as evil as he can be.

But how much money do you save or what were the reasons given? You raised the question. What were the reasons given? Were you given an explanation?

Mr. HART. No, no.

Mr. BAILEY. Can you postulate as to why, Mr. Alberger, any of you, can you help me? You do not want to postulate?

Mr. ALBERGER. I think it is difficult for us to get into an area of judging how policy decisions were made.

Mr. BAILEY. It is tough for me, I will tell you.

Mr. ALBERGER. About all that can occur is that Mr. Hart, as he indicated, did raise that as a matter of concern. And really a question about why it did not occur is better directed to those who made the decision.

Mr. BAILEY. A little bit of subjective feeling comes through on your part, just a little bit. Why do you think it should be, assuming that you think it should be? Why do you not argue why you think it should be?

Mr. ALBERGER. Why should there be a study?

Mr. BAILEY. Yes; why should they ask your advice on this?

Mr. ALBERGER. Well, it would, as it has in the past, provide at least a record that would indicate what areas there might be potential problems in. I presume that would help the policymakers prepare for the eventuality of those problems occurring. That has been the experience in the past with the generalized system of preferences investigations and on the MTN probable effects analysis we did for this committee and the Senate Finance Committee.

Mr. BAILEY. It would not be much of a public issue, I suppose, because you and the chairman seem to establish it is not going to be some type of a public thing. Would it come to this committee, the subcommittee, or the Congress?

Mr. ALBERGER. If the Congress asked for it.

Mr. BAILEY. And other laws, if they asked that?

Mr. ALBERGER. Congress in the past has asked for that and did on the MTN negotiations for analysis of the impact of the proposed tariff reductions. Both this committee and the Senate Finance asked this committee to do a substantial analysis of the effect of all the tariff reductions, and we did supply that. As I recall, we supplied it initially on the terms the committee asked for it on a confidential basis. Each committee released it publicly, as I recall. I think it was immediate.

We do it essentially for our clients, for you, and for the U.S. Trade Representatives Office, and it is their judgment whether it becomes public or not. We cannot really make that decision when we are doing the project for somebody else.

Mr. BAILEY. You are objective about it.

Mr. ALBERGER. Right.

Mr. BAILEY. I do not mean to sound catty, and obviously I am doing that on purpose. I do not think they are right in taking that approach. I really do not. I think that is just going to make more people in the public angry, and it does not help us write policy. I think you are a thousand percent right. It gives the Executive a little more freedom obviously, but it certainly does not give the voter in the street any more of an increase in the trust he might have in his Government and what it does. So I am going to assume that you feel that you ought to be asked or at least you say you have been in the past, and will ask them if maybe they will try to consider those kinds of changes or something.

I thank you. I thank you, Mr. Chairman.

Chairman GIBBONS. Thank you, gentleman.

Mr. ALBERGER. Thank you.

Chairman **Gibbons**. Our last witness for the day is Mr. Gregory Ballentine, who represents the Department of the Treasury.

STATEMENT OF J. GREGORY BALLENTINE, DEPUTY ASSISTANT SECRETARY FOR TAX ANALYSIS, DEPARTMENT OF THE TREASURY, ACCOMPANIED BY ALAN GRANWELL

Mr. **Ballentine**. Mr. Chairman and members of the committee, I will read only a summary of my testimony, if I may submit the entire testimony for the record.

I am pleased to have the opportunity to appear before this subcommittee in support of the Caribbean Basin Economic Recovery Act.

As the President noted in his transmittal message, this act is an integrated program designed to improve the lives of the people of the Caribbean Basin. The tax provisions of the act are a vital element of this integrated program.

The tax incentives in this legislation may be divided into two parts: The investment tax credit designed to promote investment in Caribbean Basin countries; and the investment tax credit and other tax incentives designed to restore the favored tax status of Puerto Rico and the U.S. Virgin Islands as well as the other U.S. possessions.

I will first address the Caribbean Basin aspects of the legislation.

To be effective, a U.S. tax incentive must cause more U.S. investment to take place in the Caribbean Basin than would otherwise occur. An effective incentive should also attract projects which will continue to benefit the recipient economy after the expiration of the incentive period.

The incentive should promote an increase in local production and employment in the Caribbean Basin rather than simply encouraging transfers of financial or intangible assets. This can best be achieved by encouraging investment in real physical capital.

The act includes an unprecedented extension for 5 years of the investment tax credit to property which is used predominantly in certain Caribbean Basin countries and which would otherwise qualify for the domestic investment tax credit.

A Caribbean Basin country will qualify for this benefit if, first, it has been designated by the President as a country entitled to the benefits of the act; and second, it enters into a bilateral executive agreement with the United States for exchange of information for tax administration purposes.

The sunset provision reiterates that this is a special measure intended to provide economic assistance in an extraordinary situation. At the end of 5 years consideration may be given to an extension of the credit on a bilateral basis through tax treaty.

A wage subsidy and tax sparing, along with the investment tax credit, were considered as possible incentives for the Caribbean Basin. Since the Caribbean Basin needs to develop the skills of its indigenous labor force, a labor-oriented subsidy has considerable intuitive appeal. A country merely tends to become dependent on the wage subsidy however with little prospect for the type of growth and development that will lead toward economic self-sufficiency.

Tax sparing is often proposed as an investment incentive for regions like the Caribbean. Tax sparing allows a credit against domestic taxes for taxes an investor is spared from paying when a foreign country reduces or waives tax liabilities as an investment incentive.

There are two major economic objections to tax sparing as an investment incentive. The first is that tax sparing is a reward to profits earned during the incentive period, regardless of whether such profits come from prior or new investments. Second, tax sparing invites nonproductive investments, such as the transfer of financial or other intangible assets and the assignment of artificially high profits to such assets.

In contrast, the investment tax credit will encourage the placement of machinery and equipment in the Caribbean Basin. The credit depends directly on the investor making a productive investment in the Caribbean Basin. By providing workers with additional capital, it will increase labor productivity and economic growth and development in the region.

Finally, the investment tax credit is independent of the foreign tax credit, requires no revenue sacrifice by the developing countries, and is relatively simple.

I want to turn briefly to some of the important details of the proposal.

A Caribbean Basin country which is designated by the President as eligible for the benefits of the act will qualify for the extension of the credit only if the country enters into a bilateral executive agreement with the United States to exchange such information as is necessary and appropriate to carry out and enforce the tax laws of the two countries.

A predominant use restriction will be applied for the credit. Only property used predominantly in one or more qualifying Caribbean Basin countries is made eligible for the credit. If property or equipment is located in a qualifying Caribbean Basin country during more than 50 percent of the taxable year, the predominant use test will be satisfied.

There will be a passthrough of the credit to 5-percent U.S. shareholders of foreign corporations. Under present law the credit would not be available to a U.S. shareholder that makes an equity investment in a foreign corporation that invests in qualifying property. Where, for reasons of local law or accepted business practice, it is necessary that the business activity be carried on through a host country corporation; that is, the business activity in the Caribbean Basin—allowance of the credit solely with respect to property owned directly by a U.S. person would not constitute an effective investment incentive.

To surmount this problem and insure the effectiveness of the credit as an investment incentive, we have designed a passthrough mechanism which would allow the credit on a current basis to a U.S. shareholder that owns 5 percent or more in value of a foreign corporation's stock, subject to certain limitations.

The passthrough credit is limited to the amount of the shareholder's actual additional equity investment in the corporation after the date of enactment of the act—actual new investment equity that goes down to the corporation.

These limitations on the passthrough credit take into account the concern that the credit is allowed currently while income earned by a foreign corporation is generally not subject to U.S. taxation until it is repatriated as a dividend to the U.S. shareholder.

It is for this reason that the passthrough credit is not allowed with respect to investment of retained earnings of the foreign corporation in Caribbean Basin property. The foreign corporation's investment must be attributable directly or indirectly to the new equity investment by the U.S. shareholder. This protects against the possibility of an initial profitable investment generating a continuous series of credits for a shareholder while U.S. tax on the income generated by such investment is deferred.

The 5-year extension of the credit that I have described is an innovative, carefully targeted incentive for new physical investment in Caribbean Basin countries. Its revenue cost will be about $50 million in 1983.

The extension of the investment tax credit for Caribbean Basin property is not inconsistent with the administration's strong policy against use of our tax treaties for conduit investments in the United States by residents from countries other than our treaty partner. Our opposition to such tax treaty abuse is sound international tax policy and consistent with the objectives of our Caribbean Basin Initiative. The purpose of the initiative is served by encouraging increases in productive economic activity and self-sustaining growth in the Caribbean Basin countries. The purpose is not served by creating or sustaining tax haven activity which is contrary to U.S. tax treaty policy, undermines the operation of the U.S. Internal Revenue Code, and fosters an increased dependence by the tax haven country on the United States.

I want to turn now to the tax proposals which affect Puerto Rico and other U.S. possessions.

As an essential counterpart to the proposals to assist Caribbean Basin countries, the act includes important tax incentive and revenue measures for Puerto Rico and the Virgin Islands. Some of these measures will also benefit other U.S. possessions.

Puerto Rico and the U.S. Virgin Islands have a special and historic relationship with the United States which this administration recognizes and values. U.S. tax policy has long extended favored tax treatment to investment in Puerto Rico, the Virgin Islands, and other U.S. possessions.

The passage of the Economic Recovery Act of 1981 [ERTA], however, substantially but unintentionally reduced the effectiveness of these incentives. Further, making the investment tax credit available to investment in qualifying Caribbean Basin countries will encourage investment in the Caribbean Basin, possibly to the detriment of Puerto Rico and the U.S. Virgin Islands.

To adjust for the impact of ERTA and the Caribbean Basin Initiative, the administration is proposing to extend certain tax incentives for investment to the U.S. possessions and to modify the rum excise tax payment arrangements with Puerto Rico and the U.S. Virgin Islands.

The encouragement of manufacturing investment in Puerto Rico is a longstanding tenet of Federal tax policy, rooted in the belief that increased capital investment is the most effective way of encouraging real economic growth in Puerto Rico.

Generally speaking, the Federal tax laws have encouraged Puerto Rican investment by exempting income from such investment from U.S. taxation. Puerto Rico has, in turn, granted tax holidays for most manufacturing operations. Thus, United States manufacturing corporations operating in Puerto Rico generally pay little or no United States or Puerto Rican tax.

Prior to the passage of the Economic Recovery Tax Act of 1981, section 936 provided a significant incentive to invest in Puerto Rico compared to the United States. By reducing the effect of the corporate tax burden on U.S. investment through the accelerated cost recovery system and liberalizing the investment tax credit, ERTA erodes the relative value of the Puerto Rican tax incentive.

Once the provisions of ERTA are fully effective, a substantial amount of U.S. investment will be taxed nearly as favorably as Puerto Rican investments, thus limiting any tax incentive for investing in Puerto Rico.

The administration proposes to restore the incentive to invest in Puerto Rico by extending the benefits of ACRS and the investment tax credit to U.S. corporations operating in Puerto Rico and the other possessions. Restoration of the incentive will require that the full investment tax credit plus one-half of the ACRS deductions be made available to a U.S. corporation owning a section 936 corporation.

These investment incentive provisions will reduce the cost of capital and promote real economic growth in Puerto Rico, the U.S. Virgin Islands, and other U.S. possessions. This proposal will restore the relative preference for investment in Puerto Rico that existed prior to the passage of ERTA. It reaffirms the congressional policy of encouraging investment in Puerto Rico and provides a significant incentive to invest in the plant and equipment which is vital to economic growth of the possessions. Its revenue cost will be about $55 million in 1983, rising to about $100 million annually by 1985.

Under present law, the Internal Revenue Code imposes an excise tax on rum. All taxes collected under the Internal Revenue Code on rum produced in Puerto Rico or the U.S. Virgin Islands and transported to the United States are paid to Puerto Rico or the U.S. Virgin Islands Governments, respectively.

At present, Puerto Rico and the Virgin Islands supply about 90 percent of the U.S. rum market. Rum produced in Puerto Rico and the U.S. Virgin Islands enters the United States duty free. The reduction in import duties on rum produced in other Caribbean Basin countries, provided for in the trade title of the act, will reduce the Puerto Rican and U.S. Virgin Islands' share of the U.S. rum market. This will adversely affect the rum industry in Puerto Rico and the U.S. Virgin Islands and reduce the amount of U.S. excise tax collections which they receive.

In order to maintain this revenue source for the islands, the legislation provides that all excise taxes collected at the current tax rates on rum imported into the United States from any country will be paid over to the treasuries of Puerto Rico and the U.S.

Virgin Islands. The estimated revenue cost of this provision is about $18 million in 1983.

Thank you, Mr. Chairman.

[The prepared statement follows:]

STATEMENT OF J. GREGORY BALLENTINE, DEPUTY ASSISTANT SECRETARY (TAX ANALYSIS), DEPARTMENT OF THE TREASURY

Mr. Chairman and Members of the subcommittee, I am pleased to have the opportunity to appear before your Subcommittee in support of the Caribbean Basin Economic Recovery Act. As the President noted in his transmittal message, this Act is an integrated program designed to improve the lives of the peoples of the Caribbean Basin. The tax provisions of the Act are a vital element of this integrated program.

The tax incentives in this legislation may be divided into two parts: the investment tax credit designed to promote investment in Caribbean Basin countries and the investment tax credit and other tax incentives designed to restore the favored tax status of Puerto Rico and the U.S. Virgin Islands, the two U.S. possessions in the region, as well as the other U.S. possessions. I will first address the Caribbean Basin aspects of the legislation. Before discussing the specifics of the legislation, it will be useful to describe the economic characteristics of the region and the current levels of U.S. investment in the region. My discussion of the parts of the legislation pertaining to Puerto Rico and other U.S. possessions will also include a review of the relevant economic context of these proposals.

I. THE CARIBBEAN BASIN—ECONOMIC CHARACTERISTICS OF THE CARIBBEAN BASIN

The term "Caribbean Basin" as used in this discussion describes those Caribbean countries which are designated by the President as qualifying for the benefits of the Act. These may include Guyana, Surinam, and countries in Central America and the Caribbean islands. My remarks will be with reference to all the countries in the region with the exception of Cuba. Although by any reasonable standard all of the qualifying jurisdictions woud be classified as developing countries, they are not a homogeneous group. They share certain features, such as low per capita income, high unemployment, lack of skilled labor, dependence on one or a few primary products, very little manufacturing activity, and small markets. But they vary widely in resources, institutions, and facilities for foreign investment.

A few countries have profitable mineral resources (oil in Trinidad and Tobago and bauxite in Jamaica, Suriname, and Guyana). Some have a reasonably sound agricultural base (the Dominican Republic and Guatemala). Some have developed trade or services sectors (Panama and Costa Rica). Some (the British Virgin Islands, the Cayman Islands, the Bahamas, and the Netherlands Antilles) are able to generate income from marketing tax savings to nonresidents. Others have practically no cash economy (Barbuda, St. Lucia, and St. Vincent). Although tourism is a major industry in the region, it cannot be relied on to support the economies of all the Caribbean countries. Some are not independent countries, but dependencies of the United Kingdom (e.g., the British Virgin Islands) or part of the Netherlands (Netherlands Antilles).

The languages spoken include Dutch, English, French, Spanish, and various dialects. The currency units differ. Communications and transportation facilities range from extremely poor to excellent. Political and economic stability vary, but are generally fragile. The total population of the area, 41 million, is governed by over 20 separate governments. The most populous country is Guatemala, with about 7 million inhabitants; the smallest are the Turks and Caicos Islands, with less than 10,000 persons. Per capita income varies from less than $300 per year in Haiti and St. Vincent to more than $3,000 annually in the Bahamas and Trinidad and Tobago. A discouraging demographic factor is the high percentage of the population under 15 years old which is dependent for support upon a relatively unskilled work force.

U.S. INVESTMENT IN THE CARIBBEAN BASIN

At the end of 1980, U.S. direct investment (equity investment in foreign affiliates plus net outstanding loans to foreign affiliates) in the Caribbean Basin jurisdictions had a value of $10.2 billion, ignoring the Netherlands Antilles where a negative investment was recorded due to the borrowings of U.S. parent corporations through Netherlands Antilles affiliates. Of that amount, $5.9 billion, or 60 percent, was in the Bahamas and Panama. Of the remaining $4.3 billion in investment, about $1.0 billion was in Trinidad and Tobago, $2.3 billion in Jamaica, the other Caribbean islands, Guyana, and Suriname, and the remaining $1.0 billion in Central American countries. A significant portion of the investment in Jamaica, Suriname, and Trinidad and Tobago is in mining (bauxite) or petroleum. U.S. direct investment in manufacturing in the region at the end of 1980 was about $1.0 billion, or approximately 10 percent of the total U.S. investment. Over 70 percent of the investment classified as manufacturing was in Panama and the Bahamas. Majority owned Caribbean basin affiliates of U.S. companies planned about $680 million in capital expenditures during 1980, of which $480 million was in mining and petroleum and $65 million in manufacturing.

II. OUTLINES OF THE PROPOSAL—REQUIREMENTS OF AN EFFECTIVE TAX INCENTIVE

To be effective, a U.S. tax incentive must cause more U.S. investment to take place in the Caribbean Basin than would otherwise occur. An incentive does this by raising the rate of return on investments, making some profitable which were previously unacceptable. An effective incentive should also attract projects which will continue to benefit the recipient economy after the expiration of the incentive period. The incentive should promote an increase in local production and employment in the Caribbean Basin, rather than simply encouraging transfers of financial or intangible assets. This can best be achieved by encouraging investment in real physical capital. An increased transfer of financial assets to the Caribbean Basin will contribute to economic growth in the Caribbean only if it increases the amount of physical investment or reduces its cost. This growth objective will be frustrated if the increased inflow of funds into the Caribbean is offset by an increased outflow of funds for investment outside the Caribbean.

DESCRIPTION OF THE PROPOSED LEGISLATION

The Act includes an unprecedented extension for five years of the investment tax credit to property which is used predominantly in certain Caribbean Basin countries and which would otherwise qualify for the domestic investment tax credit. A Caribbean Basin country will qualify for this benefit if, first, it has been designated by the President as a country entitled to the benefits of the Act, and second, it enters into a bilateral executive agreement with the United States for exchange of information for tax administration purposes.

The rules and limitations which apply to the allowance of the investment tax credit for property used predominantly in the United States will generally apply to Caribbean Basin property. The regular investment credit is generally available for up to ten percent (10 percent) of the cost of tangible personal property and other tangible property (generally not including buildings or structural components) used in connection with manufacturing, production, agriculture or certain other activities. A few narrow categories of property, such as qualified rehabilitated buildings and qualified timber property, will not be eligible for the credit if located in a Caribbean Basin country because of the specific statutory provisions governing their eligibility for the credit. In our judgment, it is not advisable to extend the credit for these specialized categories of property.

The sunset provision reiterates that this is a special measure intended to provide economic assistance in an extraordinary situation. At the end of five years consideration may be given to an extension of the credit on a bilateral basis through a tax treaty.

RELATIVE ADVANTAGES OF THE INVESTMENT TAX CREDIT

A wage subsidy and tax sparing, along with the investment tax credit, were considered as possible incentives for the Caribbean Basin. Since the Caribbean Basin needs to develop the skills of its indigenous labor force, a labor oriented subsidy has considerable intuitive appeal. This type of incentive, however, does not increase the capital-labor ratio and therefore it does not improve the long run productivity of the labor force. It is a temporary incentive that ceases to have effect as soon as wages are no longer subsidized. A country merely tends to become dependent on the wage subsidy, with little prospect for the type of growth and development that will lead toward economic self-sufficiency. The recipient countries themselves may resent a wage subsidy. They may view it as a "colonialistic" attempt by the United States to restrict the Caribbean Basin to the role of a supplier of low wage goods. For these reasons, it is preferable to rely on a capital incentive which indirectly encourages the employment of more labor and which will improve the overall productivity of labor.

Tax sparing is often proposed as an investment incentive for regions like the Caribbean. Tax sparing allows a credit against domestic taxes for taxes an investor is spared from paying when a foreign country reduces or waives tax liabilities as an investment incentive. There are two major economic objections to tax sparing as an investment incentive. The first is that tax sparing is a reward to profits earned during the incentive period, regardless of whether such profits come from prior or new investments. That is, no new investment is needed to obtain the benefits. Thus, there is no assurance that tax sparing will contribute to economic growth by increasing real physical capital investment in the recipient country. Secondly, tax sparing invites non-productive investments, such as the transfer of financial or other intangible assets and the assignment of artifically high profits to such assets, in order to generate tax spared income.

In contrast, the investment tax credit which we are proposing will encourage the placement of machinery and equipment in the Caribbean Basin. The credit depends directly on an investor making a productive investment in the Caribbean Basin. By providing workers with additional capital, it will increase labor productivity and economic growth and development in the region.

Finally, the investment tax credit is independent of the foreign tax credit, requires no revenue sacrifice by the developing countries, and is relatively simple. Potential U.S. investors in the Caribbean Basin region are familiar with the credit as it applies to domestic investments. Its effectiveness will not be undercut by the uncertainty which would accompany any totally new incentive.

III. DETAILS OF THE PROPOSAL—QUALIFYING CARIBBEAN BASIN COUNTRIES

A Caribbean Basin country which is designated by the President as eligible for the benefits of the Act will qualify for the extension of the credit only if the country enters into a bilateral executive agreement with the United States to exchange such information as is necessary and appropriate to carry out and enforce the tax laws of the two countries.

Exchange of tax information assists the administration of the tax laws of both the United States and the qualifying country. The tax administrators of the Caribbean Basin countries will have access to information from the IRS regarding their taxpayers who engage in economic activities in the United States and thereby should strengthen their own tax administration. This self-help aspect of the measure is consistent with the overall concept of the Caribbean Basin Initiative. Moreover, the United States will itself require access to such information to adequately administer the tax credit, particularly where a "pass-through" credit is claimed by a five percent (5 percent) or greater U.S. shareholder in a foreign corporation. (The "pass-through" aspect of the proposal is discussed below.)

In addition, several countries in the Caribbean Basin region are tax havens which have been used both for avoidance and evasion of U.S. tax laws. We do not believe that it is appropriate for countries to benefit from U.S. tax incentives unless they are willing to cooperate with the United States in matters of tax administration.

EXCHANGE OF INFORMATION AGREEMENTS

The legislation authorizes the Secretary of the Treasury to negotiate and conclude the exchange of information agreements. While the Secretary is accorded discretion regarding what kinds of information will be included within the scope of the exchange of information provisions, the Act imposes certain minimum standards for such agreements.

The exchange of information provisions in the agreements must include within their scope tax information pertaining to "third-country persons," that is, nationals or residents of countries other than the United States or the Caribbean Basin country that is a party to the agreement. This approach is consistent with our present tax treaty policy, embodied in Article 26 of the U.S. Model Income Tax Treaty. In accordance with that policy, a jurisdiction with restrictions on disclosure of information regarding such third country persons would be required to modify such restrictions. The same principle applies with respect to disclosure of information regarding ownership of bank accounts or share ownership. Most countries do not place restrictions on disclosure of such information; such limitations are characteristic primarily of jurisdictions which have organized themselves as tax havens.

The exchange of information agreements will be terminable on reasonable notice by either party. This will permit the credit to be terminated with respect to future investment in the event that the President revokes his designation of the country as a country eligible for the benefits of the Act.

The Secretary may incorporate by reference in an exchange of information agreement the exchange of information provisions of an existing income tax treaty with a Caribbean Basin country, provided such treaty provisions otherwise satisfy the requirements of the statute. Our more recent tax treaties, such as the recently ratified treaty with Jamaica, will satisfy such standards and we would be desirous of extending this tax incentive to these treaty partners as expeditiously as possible. It should be clearly understood that exchange of information agreements may be entered into with a country whether or not the country has a tax treaty with the United States.

It is expected that the exchange of information agreements will generally become effective on signature. The text of the agreements will, of course, be transmitted to Congress not later than sixty days after the agreement has been signed, in accordance with the prescriptions of the Case Act (1 U.S.C. section 112b).

PREDOMINANT USE

Property used predominantly outside the United States generally is not eligible for the investment tax credit. The Act establishes an additional exception to this rule for Caribbean Basin property; that is, property used predominantly in one or more qualifying Caribbean Basin property will be subject to recapture if the property is used predominantly outside one or more qualifying Caribbean Basin countries is made eligible for the credit.

Under existing Treasury regulations the test for determining predominant use is the physical location test. Thus, if property or equipment is located in one or more qualifying Caribbean Basin countries during more than 50 percent of the taxable year, the predominant use test will be satisfied. The same regulations also provide that the determination of whether a credit is allowable with respect to any property is made only with respect to the year the property is placed in service. If property is thereafter used predominantly outside the United States the credit taken with respect to such property will be subject to recapture. A credit taken with respect to qualifying Caribbean Basin property will be subject to recapture if the property is used predominantly outside one or more qualifying Caribbean Basin countries and the United States.

The Act provides an exception to this recapture rule in the case where a qualifying Caribbean Basin country no longer constitutes a qualifying country because the President's designation of the country as eligible for the benefits of the Act is terminated or the exchange of information agreement is terminated. In such a circumstance, property which continues to be used predominantly in the country in succeeding taxable years without interruption will not be subject to the recapture rules. It would not be equitable to subject the credit for such property to recapture because of an event which is not within the taxpayer's control.

PASS-THROUGH OF CREDIT TO 5 PERCENT U.S. SHAREHOLDER OF FOREIGN CORPORATION

To summarize my discussion to this point, the credit will be allowed to a U.S. citizen, resident, or corporation that invests in property that is used predominantly in one or more qualifying Caribbean Basin countries after the enactment of the Act. Under present law, however, the credit would not be available to a U.S. shareholder that makes an equity investment in a foreign corporation that invests in qualifying property. Where, for reasons of local law or accepted business practice, it is necessary that the business activity be carried on through a "host country" corporation, allowance of the credit solely with respect to property owned directly by a U.S. person would not constitute an effective investment incentive.

To surmount this problem and ensure the effectiveness of the credit as an investment incentive, we have designed a pass-through mechanism which would allow the credit on a current basis to a U.S. shareholder that owns five percent or more in value of a foreign corporation's stock, subject to certain limitations.

The pass-through credit is computed with respect to the shareholder's pro rata share of the foreign corporation's investment in Caribbean Basin property. The shareholder's pro rata share of such investment is limited for this purpose, however, to the amount of the shareholder's actual additional equity investment in the corporation after the date of enactment of the Act. The purpose of this limitation is to key the incentive in these circumstances to new equity investment which is permanent in nature and subordinate to debt claims or trade payables. In our view, new equity investment is the kind of investment which is likely to be responsive to the credit and which will form the base for continued future growth in the Caribbean Basin economies.

The limitations on the pass-through credit also take into account the concern that the credit is allowed currently while income earned by a foreign corporation is generally not subject to U.S. taxation until it is repatriated as a dividend to the U.S. shareholder. It is for this reason that the pass-through credit is not allowed with respect to investment of retained earnings of the foreign corporation in Caribbean Basin property. The foreign corporation's investment must be attributable, directly or indirectly, to new equity investment by the U.S. shareholder. This protects against the possibility of an initial profitable investment generating a continuous series of credits for a shareholder while U.S. tax on the income generated by such investment is deferred.

SUMMARY VIEW OF INVESTMENT TAX CREDIT

The five year extension of the credit I have described is an innovative, carefully targeted incentive for new physical investment in Caribbean Basin countries. This proposal represents as powerful a tax incentive for investment as is feasiable without disturbing the integrity of our tax system. Its revenue cost will be about $50 million in 1983.

RELATION OF EXTENSION OF CREDIT TO U.S. TAX TREATIES

The United States has a number of tax treaties with countries in the Caribbean Basin region, including extensions of certain of our older treaties with the United Kingdom and the Netherlands. It is our longstanding tax treaty policy to provide U.S. source basis tax benefits to the residents of the treaty partner and to obtain tax benefits for U.S. residents. We do not, as a general rule, limit our residence basis taxation of our citizens and residents. The decision to provide a tax credit incentive for investment in qualifying Caribbean Basin countries is generally at variance with our treaty policy of not limiting (or reducing) U.S. taxation of our citizens and residents. This decision highlights the special nature of our relationship to the Caribbean Basin region and the importance we attach to this Initiative.

Countries outside the Caribbean Basin region will, no doubt, seek similar benefits through tax treaties. The United States has exchanged notes with a number of developing country tax treaty partners in which we acknowledge the partner's desire to include investment incentives in the treaty, but state that the United States is not in a position to agree to such incentives. The letters go on to state that if policies change in this regard in the future, the United States will reopen discussions with a view to amending the treaty to include an investment incentive. These countries may view the extension of the tax credit as such a change in our policy. A decision regarding further extensions of the investment tax credit, both to existing and new treaty partners, would not be made without full consultation with interested Congressional committees.

The extension of the investment tax credit for Caribbean Basin property is not inconsistent with this Administration's strong policy against use of our tax treaties for conduit investments in the United States by residents from countries other than our treaty partner. Our opposition to such tax treaty abuse is sound international tax policy and consistent with the objectives of our Caribbean Basin Initiative. The purpose of the Initiative is served by encouraging increases in productive economic activity and self-sustaining growth in the Caribbean Basin countries. This purpose is not served by creating or sustaining tax haven activity which is contrary to U.S. tax treaty policy, undermines the operation and administration of the Internal Revenue Code, and fosters an increased dependence by the tax haven country on the United States.

IV. PUERTO RICO AND OTHER U.S. POSSESSIONS

As an essential counterpart to the proposals to assist Caribbean Basin countries, the Act includes important tax incentive and revenue measures for Puerto Rico and the U.S. Virgin Islands. Some of these measures will also benefit other U.S. possessions.

BACKGROUND OF THE LEGISLATIVE MEASURES AFFECTING THE POSSESSIONS

Puerto Rico and the U.S. Virgin Islands have a special and historic relationship with the United States which this Administration recognizes and values. U.S. tax policy has long extended favored tax treatment to investment in Puerto Rico, the U.S. Virgin Islands and other U.S. possessions. The passage of the Economic Recovery Act of 1981 (ERTA), however, substantially, but unintentionally, reduced the effectiveness of these incentives. Further, making the investment tax credit available to investment in qualifying Caribbean Basin countries will encourage investment in the Caribbean Basin, possibly to the detriment of Puerto Rico and the U.S. Virgin

Islands. It is essential that Puerto Rico and the U.S. Virgin Islands share in the expected economic progress, growth, and stability in this region. Special investment incentives must be provided for these possessions so that the development in the Caribbean Basin induced by the Initiative does not occur at the expense of Puerto Rico or the Virgin Islands.

The importance of the measures contained in this legislation is underscored by the adverse economic situation facing Puerto Rico. The Puerto Rican unemployment rate is approximately 22 percent, with no immediate prospect of decreasing. Investment in plant and equipment in 1980, after adjusting for inflation, was only one-half the value of investment in 1970. Between 1980 and 1981, the number of contractual agreements between the Puerto Rican Economic Development Administration and potential non-local investors dropped sharply. This drop in new contractual agreements indicates that the number of manufacturing plants beginning operation in Puerto Rico in the immediate future is likely to fall.

To adjust for the impact of ERTA and the Caribbean Basin Initiative, the Administration is proposing to extend certain tax incentives for investment to the U.S. possessions and to modify the rum excise tax payment arrangements with Puerto Rico and the U.S. Virgin Islands. Although the tax incentives will be available to the U.S. Virgin Islands and all other possessions, their principal impact will be with regard to business operations in Puerto Rico.

EXISTING U.S. TAX POLICY TOWARD PUERTO RICO

The encouragement of manufacturing investment in Puerto Rico is a longstanding tenet of Federal tax policy. This principle is rooted in the belief that increased capital investment is the most effective way of encouraging real economic growth in Puerto Rico. Generally speaking, the Federal tax laws have encouraged Puerto Rican investment by exempting income from such investment from U.S. taxation. Puerto Rico has, in turn, granted tax holidays for most manufacturing operations. Thus, U.S. manufacturing corporations operating in Puerto Rico generally pay little or no U.S. or Puerto Rican tax.

Under section 936 of the Code, a U.S. corporation (the 936 corporation) deriving income from Puerto Rico is subject to Federal tax on its worldwide income, but a special credit available under section 936 fully offsets the Federal tax on income from a trade or business in Puerto Rico or from "qualified possessions source investment income." A U.S. corporation which owns at least 80 percent of a section 936 corporation is also exempt from Federal tax on the dividend income from the 936 corporation. Since 1948, Puerto Rico has had a complementary program of tax exemption, called Operation Bootstrap, under which exemptions from Puerto Rican tax have been offered as incentives to U.S. companies to invest in manufacturing plants in Puerto Rico.

Prior to the passage of the Economic Recovery Tax Act of 1981, section 936 provided a significant incentive to invest in Puerto Rico compared to the United States. By reducing the effective corporate tax burden on U.S. investment through the Accelerated Cost Recovery System (ACRS) and liberalizing the investment tax credit, ERTA erodes the relative value of the Puerto Rican tax incentive. Once the provisions of ERTA are fully effective, a substantial amount of U.S. investment will be taxed nearly as favorably as Puerto Rican investments, thus eliminating any tax incentive for investing in Puerto Rico. The Administration proposes to restore the incentive to invest in Puerto Rico by extending the benefits of ACRS and the investment tax credit to U.S. corporations operating in Puerto Rico and the other possessions. Restoration of the incentive will require that the full investment tax credit plus one-half of the ACRS deductions be made available to a U.S. corporation owning a section 936 corporation.

DESCRIPTION OF TAX INCENTIVES

Under present law, property used predominantly outside the United States generally is not eligible for the investment tax credit. However, property owned by a domestic corporation and used predominantly in a U.S. possession qualifies for the credit unless the domestic corporation has in effect an election to claim a Puerto Rico or possession tax credit under section 936 (a section 936 corporation) or is entitled to the benefits of section 934(b), relating to reduction in tax liability incurred to the Virgin Islands (a section 934(b) corporation). Also, property owned by a U.S. citizen and used predominantly in a U.S. possession qualifies for the credit unless the U.S. citizen is entitled to the benefits of Code sections which limit U.S. taxation of income derived in a U.S. possession. The Caribbean Basin Economic Recovery Act would allow the investment tax credit for any property owned by a section 936 or

934(b) corporation or by a U.S. citizen entitled to the benefits of such Code sections and which is used predominantly in a possession of the United States. The Act also provides that property used in a possession would be eligible for the recovery lives generally available for property not used predominantly outside the U.S. Thus, it will extend ACRS to property used in a possession.

Because section 936 and 934(b) corporations would be unable to use these tax benefits, the Act provides for a pass-through of the investment tax credit and fifty percent of the cost recovery deductions attributable to property owned by a section 936 or a domestic section 934(b) corporation to certain U.S. corporations that together own 80 percent or more of the stock of the section 936 or 934(b) corporations. Thus, a U.S. corporation that would be a member of an affiliated group that includes the section 936 or domestic 934(b) corporation (but for special rules excluding section 936 and 934(b) corporations from an affiliated group), would be allowed the investment tax credit and fifty percent of the cost recovery deductions otherwise allowable to the section 936 or domestic 934(b) corporation.

EFFECT OF PROPOSAL

These investment incentive provisions will reduce the cost of capital and promote real economic growth in Puerto Rico, the U.S. Virgin Islands, and other U.S. possessions. This proposal will restore the relative preference for investment in Puerto Rico that existed prior to the passage of ERTA. It reaffirms the Congressional policy of encouraging investment in Puerto Rico and provides a significant incentive to invest in the plant and equipment which is vital to economic growth of the possessions. Its revenue cost will be about $55 million in 1983, rising to $100 million annually by 1985.

DISPOSITION OF EXCISE TAXES ON RUM

Under present law, the Internal Revenue Code imposes an excise tax on rum. All taxes collected under the Internal Revenue Code on rum produced in Puerto Rico or the U.S. Virgin Islands and transported to the United States (less the estimated amount necessary for payment of refund and drawbacks), are paid to Puerto Rico or the U.S. Virgin Islands, respectively.

At present, Puerto Rico and the U.S. Virgin Islands supply about 90 percent of the U.S. rum market. Rum produced in Puerto Rico and the U.S. Virgin Islands enters the United States duty free. The reduction in import duties on rum produced in other Caribbean Basin countries, provided for in the trade title of the Act, will reduce the Puerto Rican and U.S. Virgin Islands' share of the U.S. rum market. This will adversely affect the rum industry in Puerto Rico and the U.S. Virgin Islands and reduce the amount of U.S. excise tax collections which they receive.

In order to maintain this revenue source for the islands, the legislation provides that all excise taxes collected at the current tax rates on rum imported into the United States from any country (less the estimated amount necessary for payment of refunds and drawbacks) will be paid over to the treasuries of Puerto Rico and the U.S. Virgin Islands. The amount per proof gallon paid over will not exceed the amount per proof gallon which would have been paid over if the rum had been produced in Puerto Rico or the U.S. Virgin Islands. The Secretary of the Treasury will prescribe by regulations a formula for the division of these tax collections between Puerto Rico and the U.S. Virgin Islands. The estimated revenue cost of this provision is about $18 million in 1983.

Chairman GIBBONS. Thank you, sir.

You are into one of the most complicated areas of this entire package here. Would you explain to me how this will work? I am talking to you now about the investment tax credit for the Caribbean Basin, not to Puerto Rico or the Virgin Islands.

Just lead me through the operation, if you will, please.

Mr. BALLENTINE. It is different depending on the nature of the corporation. If it is a branch of a U.S. corporation operating in Puerto Rico then, essentially, the tax credit is no different than the tax credit as applied in the United States. It is a credit on depreciable property other than structures. It is a credit against taxes on the U.S. taxable income.

Mr. **Bailey**. Would the chairman yield? Didn't you ask how it would operate as an investment for one of the Caribbean Basin countries?

Chairman **Gibbons**. Yes.

Mr. **Bailey**. That is what I thought you asked. I share your curiosity.

Mr. **Ballentine**. Did I say Puerto Rico? I am talking about a U.S. corporation which is operating in a qualifying Caribbean Basin country. I'm sorry. If the corporation is a U.S. corporation, then the credit is as much as is normally available for domestic investment. It is creditable currently against the corporation's U.S. tax liability.

Chairman **Gibbons**. Well, isn't that already the case? I imagine these Caribbean countries have income taxes, don't they?

Mr. **Ballentine**. Certainly, but there is no credit. If a U.S. corporation places capital in a Caribbean Basin country right now there is no investment credit generated that is useful against U.S. tax liability.

Chairman **Gibbons**. In effect, what you are saying is I am a company. I invest in the Caribbean Basin. I generate a profit. That profit is taxed by the local government and I get a tax credit against my foreign income.

Mr. **Ballentine**. Under the foreign tax credit you would get a foreign tax credit.

Chairman **Gibbons**. I get a foreign tax credit, so my money comes back tax-free.

Mr. **Ballentine**. It comes back, and depending on the level of the local tax in your foreign tax credit situation, you may have no residual tax liability.

Chairman **Gibbons**. In other words, if the local tax is high enough?

Mr. **Ballentine**. Exactly; under this proposal you would get an investment tax credit.

Chairman **Gibbons**. An investment tax credit against your U.S. tax liability.

Mr. **Ballentine**. Yes; so in the United States you are operating and have a tax liability in the United States of $1 million. You have made an investment in a Caribbean Basin country which has generated a tax credit. The tax rate locally down there is above 46 percent, so that income there doesn't generate a U.S. liability because of our foreign tax credit. You nonetheless have that investment tax credit, which can be used to reduce your tax liability in the United States.

Chairman **Gibbons**. You would, in effect, flow that back through and take it against your—so this is a vast departure from our taxation of foreign profits.

Mr. **Ballentine**. Exactly right. It is an unprecedented allowance of the investment tax credit for investments made outside the United States. Now again, where there is no residual tax liability, the pass-through also applies in the case where you have paid sufficient foreign taxes to have foreign tax credits such that there is no residual liability.

If the tax rate is low there and there are not other foreign tax credits there would be a residual liability in the United States because we do tax that income and the credit would be used against that residual liability.

Mr. BAILEY. What you are simply saying is that if a company has available to them sufficient foreign tax credits that they can write off against liability here that——

Mr. BALLENTINE. Foreign liabilities.

Mr. BAILEY. But that is to be credited against American tax liability and what you are saying is that the investment tax credits in this situation would be on top of or in addition.

Mr. BALLENTINE. That is essentially right. In other words, the foreign tax credits are creditable against liabilities on foreign profits. Then, in addition to that, the investment tax credit could be allowed so if you have enough foreign tax credits that you do not pay a current liability on foreign profits you would still have the investment tax credit applied in the United States.

Mr. BAILEY. What you are saying is there is tax liability in this country if foreign tax credits and domestic tax liability are a wash, that the ITC can apply against the domestic tax liability, in addition. Is that correct?

Mr. BALLENTINE. That's correct.

Yes; it is, I should add, different now in the case of a foreign corporation. For example, say for local custom, in setting up in a country in the Caribbean Basin one instead sets up a foreign corporation rather than a U.S. branch and then the investment tax credit is only available on new equity funds put down into that foreign corporation to buy equipment.

If the foreign corporation, for example, earns profits and reinvests those in depreciable equipment, no investment tax credit is generated. It is only on new equity investments made from the U.S. corporation down to the foreign corporation.

Chairman GIBBONS. So any investment that has already been made, you would have to increase it.

Mr. BALLENTINE. You would not only have to increase it, you would have to use U.S. funds to do so, that would have already been subject to tax in the United States.

Chairman GIBBONS. That sounds logical. I assume this investment tax credit is a standard investment tax credit. It does not include biomass and all those other kinds of——

Mr. BALLENTINE. It does not include the energy tax credit, just the basic investment tax credit—essentially 3-, 5-, and 10-year equipment eligible.

Chairman GIBBONS. Does it include ships?

Mr. BALLENTINE. No; I don't believe it does. Pardon me, it could include a ship.

Mr. GRANWELL. It could include ships.

Chairman GIBBONS. Could you get a little closer to the microphone?

Mr. GRANWELL. We have an exception in our present investment tax provisions for ships used predominantly outside the United States and in the proposal ships would qualify for the investment credit if they are used within the qualifying territories, but not if they are used without the qualifying territories. So it is a delimited investment tax credit for ships.

Chairman GIBBONS. How about airplanes?

Mr. **Granwell**. Similar.

Chairman **Gibbons**. How about sailboats?

Mr. **Ballentine**. Normally a sailboat would not qualify under U.S. rules. It is not normally depreciable property in business.

Mr. **Granwell**. If it is leased and otherwise is in business, I believe it could.

Chairman **Gibbons**. Give me that one on sailboats again. I know a lot of people that own sailboats down there.

Mr. **Granwell**. If the sailboat is used for pleasure you cannot qualify for the credit, but if it is used in a commercial activity I believe it could.

Mr. **Ballentine**. If it is used for transport between islands so that it is predominantly used in the region it is treated as any other boat.

Chairman **Gibbons**. How about a sailboat that is just chartered out to people or boats with crews?

Mr. **Ballentine**. Used predominantly within the region for commercial use, I presume it would qualify.

Chairman **Gibbons**. I don't know whether when you charter a boat out to a vacationing American business person, is that a commercial use?

Mr. **Ballentine**. It would be a commercial use for the owner of the boat, yes.

Chairman **Gibbons**. In effect we will be taxing Jamaican rum and rebating that money to Puerto Rico or the Virgin Islands?

Mr. **Ballentine**. That is correct. All rum coming into the United States—the tax receipts at the existing tax rate would be rebated to Puerto Rico and the U.S. Virgin Islands. There is no attempt to make up in this for the hardships imposed upon the rum industry in Puerto Rico and the Virgin Islands and they will probably be damaged by this, but we are seeing to it that there is not an additional loss of revenue.

Chairman **Gibbons**. To the island.

Mr. **Ballentine**. To the island governments.

Chairman **Gibbons**. What was the other income tax provision you extend to the Virgins and Puerto Rico?

Mr. **Ballentine**. The investment tax credit is also extended to them, and the accelerated cost of recovery.

Chairman **Gibbons**. They already get the investment tax credit, don't they?

Mr. **Ballentine**. No, sir. That is, a passthrough to the U.S. firm. They don't get it, no.

Chairman **Gibbons**. Mr. Bailey.

Mr. **Bailey**. Thank you. Loss of revenue. What about loss of jobs? Have you done any analysis on that?

Mr. **Ballentine**. No, Mr. Bailey. We don't have a loss of jobs figure.

Mr. **Bailey**. On the rum situation, for example, you have not done any?

Mr. **Ballentine**. You mean loss of jobs in Puerto Rico and the Virgin Islands?

Mr. **Bailey**. I think we ought to think about that.

Mr. **Ballentine**. No, I don't have a figure on that loss of jobs.

Mr. Bailey. My gosh, hasn't that occurred to anybody? I mean, we have parallels for job displacement studies in current law, or what used to be an economic development administration that I talked to Mr. Waldmann about earlier.

Mr. Ballentine. It certainly has occurred. I don't know if we attempted to quantify the loss of jobs.

Mr. Bailey. How do you quantify the $55 million which you assume would be a revenue drain? I do not know whether that includes the excise tax changes and rebates, but give me the figures that you have on the ITC?

Mr. Ballentine. The ITC for the Caribbean Basin, there are two of them. I believe it is $50 million a year.

Mr. Bailey. Excise tax only amounts to $5 million?

Mr. Ballentine. There is no excise tax.

Mr. Bailey. I am talking about the rum rebate.

Mr. Ballentine. $18 million.

Mr. Bailey. What is your ITC figure? You gave me $55 and $100 million.

Mr. Ballentine. There are two investment tax credit provisions, one that applies only to the Caribbean Basin, excluding Puerto Rico and the Virgin Islands. That is $50 million.

Mr. Bailey. What does that rise to? What are your outyear figures on that?

Mr. Ballentine. I don't have a really confident extension of that number right now.

Mr. Bailey. How do you come up with that number?

Mr. Ballentine. We essentially examined the data we have on the levels of investment and made a rough and ready assumption on the effect this credit would have to increase that investment. It is approximately a 25-percent increase in investment.

Mr. Bailey. You had to have some idea about where that $50 million is going to be invested. What sector?

Mr. Ballentine. Yes, we do.

Mr. Bailey. I would like to see that information. What sectors are they?

Mr. Ballentine. I don't have it with me right now, I don't think.

Mr. Bailey. I think that is very important.

Mr. Ballentine. It is very important. I am sorry I do not have it with me, but we have looked at the past record of holdings of investments by U.S. corporations in the area.

Mr. Bailey. Your predication is that there will simply be an expansion, then?

Mr. Ballentine. That is correct. Our assumption is there will be an expansion of this. I do not think the expansion, however, will mirror the existing pattern because the existing pattern is probably heavily influenced by the existing duties and the other portions of the act alter that so much that I would not expect the same——

Mr. Bailey. That is good reasoning, but Mr. Chairman, could we ask that they report to the committee on your study on where this income was going to go, what sectors in the economy?

Mr. Ballentine. What we do have is current holdings of capital. The breakdown may not be as fine. I am certain it is not as fine as we would all like. I do not think it is much finer than manufacturing, oil, bauxite, and some minerals, but we have that breakdown and I would be happy to submit it. Bauxite is one of the main mining industries in the area.

Mr. **Bailey**. Yes, it is. I am glad you said that. I am going back to the question the chairman asked about energy. I will tell you why I am getting a little suspicious here.

Have you stumbled upon any interest on the part of aluminum countries around the world to bring the refining process to the bauxite instead of vice versa, which is technically the case today? Does that work into your study?

Mr. **Ballentine**. We know of no such particular plans, no.

Mr. **Bailey**. Let me ask you something. What are bauxite deposits in these areas? What are they?

Mr. **Ballentine**. You mean the magnitude of the——

Mr. **Bailey**. The Caribbean Basin countries, do you know what they are?

Mr. **Ballentine**. I am not sure I understand.

Mr. **Bailey**. Do they have bauxite mines in these countries now?

Mr. **Ballentine**. In a select few of them yes, they do.

Mr. **Bailey**. The ones on the northern coast of South America, I think. They have got significant amounts, don't they?

Chairman **Gibbons**. Jamaica is the main one. It is on the northern coast of Jamaica.

Mr. **Bailey**. Would the ITC's be available to investment in that type of facility?

Mr. **Ballentine**. Yes, they would, for qualifying investment in those facilities they would.

Mr. **Bailey**. I would think that they would. Did you consider that in your study?

Mr. **Ballentine**. Yes, we did.

Mr. **Bailey**. And you just viewed it in terms of an increase in the expansion of the development of the bauxite deposit, not in any kind of major movement of bauxite refining?

Mr. **Ballentine**. We did not take into account any particular pattern that that investment would take in bauxite.

Mr. **Bailey**. Did you factor in the desire expressed by some of the other donor countries to provide cheaper petroleum?

Mr. **Ballentine**. No. I don't think that has been specifically taken into account. I am not sure how we would in the kind of data that we have, that kind of precision into effecting what we would take into account as a revenue loss. I do not think we would be able to say that figure of $50 million should be, instead, $53 million or $54 million because of that kind of consideration.

We are talking about an assumption of a 25-percent increase in the investment in the region.

Mr. **Bailey**. You remember we talked about that issue here today if this thing goes through, OK?

Mr. **Ballentine**. Yes, Mr. Bailey.

Chairman **Gibbons**. Let me ask some questions. Do these tax concessions take effect immediately or do they take effect after a tax treaty has been negotiated?

Mr. **Ballentine**. They do not take effect after a tax treaty. They do take effect, however, only after an executive agreement has been signed on the exchange of information.

Chairman **Gibbons**. On access to tax information?

Mr. **Ballentine**. That is correct.

Chairman **Gibbons**. How much tax information are you going to get out of these people?

Mr. **Ballentine**. Well, we would expect to get information on banking activities and the kind of information that the Internal Revenue Service needs in a typical audit of individuals operating in that area. We would expect to get some information on third parties, on residents of third countries.

Chairman **Gibbons**. That would be a big help in the administration of taxation in the United States.

Mr. **Ballentine**. Absolutely. It is crucial to this program that we not be extending benefits until that agreement has been signed.

Chairman **Gibbons**. Does that include the Netherlands Antilles?

Mr. **Ballentine**. Countries such as the Netherlands Antilles would be subject to signing that benefit.

Chairman **Gibbons**. The Bahamas?

Mr. **Ballentine**. Yes, Mr. Chairman.

Chairman **Gibbons**. Wow.

Mr. **Ballentine**. If they do not sign it they would not be eligible for the investment tax credit.

Chairman **Gibbons**. That could be the greatest antiracketeering statute we have passed around here. [Laughter.]

Mr. **Granwell**. The information we would require, as Mr. Ballentine had indicated, would be very broad and would include information not only with respect to Antillian residents but also residents of other countries who utilize the Antilles as well as U.S. persons. It is a very broad exchange of information.

Chairman **Gibbons**. Do you expect to penetrate their Bank Secrecy Act?

Mr. **Granwell**. Yes.

Chairman **Gibbons**. I will pass this bill just on that alone. [Laughter.]

Mr. **Granwell**. If they sign the agreement.

Chairman **Gibbons**. Well, if it is good——

Mr. **Ballentine**. If it doesn't happen, they do not get the investment tax credit.

Chairman **Gibbons**. If it does not happen they do not get the benefit of it. Well, that is the way you beat crime—have something better.

OK. Well, that is fine. Thank you very much.

This concludes our hearing for the administration witnesses. We will resume on March 23 at 9:30 a.m., in room B-318 of the Rayburn House Office Building.

[Whereupon, at 5:10 p.m., the subcommittee adjourned, to reconvene at 9:30 a.m., Tuesday, March 23, 1982.]

CARIBBEAN BASIN INITIATIVE

TUESDAY, MARCH 23, 1982

House of Representatives,
Committee on Ways and Means,
Subcommittee on Trade,
Washington, D.C.

The subcommittee met at 9:40 a.m, pursuant to notice, in room 1100, Longworth House Office Building, Hon. Sam M. Gibbons (chairman of the subcommittee) presiding.

Chairman Gibbons. Good morning, ladies and gentlemen. We will come to order as soon as people can get copies of the testimony that they are seeking over there.

I welcome you again to the Subcommittee on Trade's hearing on the Caribbean Basin Initiative by the administration. We have a number of witnesses today in this room and will have a number tomorrow, and then we will finish up hearing from the private sector about this initiative in room 2203 of the Rayburn Building on Thursday.

All witnesses may understand that testimony does not necessarily have to be read in order to be in the record. All statements will appear in the record in full, and, of course, if witnesses can summarize their testimony without taking more time than it does to read it, please summarize it.

Our first set of witnesses today is from the Virgin Islands, and we have a panel composed of our colleague, the Honorable Ron de Lugo, who is a delegate to the U.S. Congress from the Virgin Islands, and we also have on that panel Mr. Juan Luis, who is the Governor of the Virgin Islands.

We welcome you here. The Virgin Islands is a beautiful place, an important place. It is part of the United States of America and we recognize our special responsibility to the people of those islands.

Mr. de Lugo, I do not know whether you want to proceed first or whether you want to introduce the Governor and have him proceed first, but you may proceed as you wish.

STATEMENT OF HON. RON DE LUGO, A DELEGATE TO THE U.S. CONGRESS FROM THE VIRGIN ISLANDS, ACCOMPANIED BY MARGARET MARTIN

Mr. de Lugo. Thank you very much. I want to thank you for your continuing concern regarding the Caribbean Basin Initiative, the courtesies that you have extended to me as delegate for the U.S. Virgin Islands, and particularly your sensitivity expressed to me of the impact of the Caribbean Basin Initiative on the U.S. territories in the Caribbean.

I have a prepared statement which I have handed in, and I will summarize.

Mr. Chairman and members of the subcommittee, Governor Luis of the Virgin Islands and myself are here today to testify regarding our concerns about the President's proposed Caribbean Basin Initiative. I recognize this committee has placed the Caribbean Basin Economic Recovery Act on a fast track in order to accommodate the President's desire to aid the region in as short an order as possible.

I agree it is important for us to focus attention on assisting our economically depressed and subsequently politically volatile neighbors. There are, however, some real concerns as to the effect this act will have on the U.S.-flag territories in the Caribbean.

In his message to Congress last Wednesday, the President stated:

> Puerto Rico and the Virgin Islands have a long-standing special relationship with the United States. Their development must be enhanced by our policy to the rest of the region. They have consulted closely with Puerto Rico and the Virgin Islands about the Caribbean Basin Initiative, and the legislation I am requesting today will reflect Puerto Rico and Virgin Island interests in many important ways.

I think it is wonderful that the President has said the U.S. Virgin Islands and Puerto Rico must be enhanced by the policy toward the Caribbean Basin. However, let's be realistic. I believe that any fair minded person would have to say that in this legislation the position of the flag territories certainly is not enhanced, and yet the fact is that we are not far from a compromise position which would allow us living in the U.S. territories to survive a Caribbean Initiative.

For the flag territories to survive this initiative, certain safeguards and additional incentives are imperative. Some of these have been incorporated into the act. The extension of the accelerated cost recovery system and investment tax credit to companies operating in the flag territories, along with the direct investment and pass-through provisions, will help to some degree to offset the impact of extending the ITC benefits to Caribbean Basin countries.

One safeguard which we stressed as a priority from the beginning of our negotiations with the administration is completion of the St. Thomas-Virgin Islands Airport. This airport has repeatedly been at the top of the Black Star airport list, one of the most dangerous airports in the world.

This, coupled with the fact there are only two airports in the Caribbean region smaller than St. Thomas, places us at a clear disadvantage in an area where access by air determines the success of tourism as well as other business development.

In the fact sheet on the President's OAS speech announcing his Caribbean policy, it was clearly stated:

> Legislation under the Caribbean Basin Initiative will reflect Puerto Rico and Virgin Islands interest in the following ways: expansion of airports in the Virgin Islands and other measures to encourage the development of Puerto Rico and the Virgin Islands as a transportation hub for the Caribbean region.

Once the ADAP bill moves out of the Ways and Means Committee, we will expect the Secretary of Transportation to honor his commitment to us to support the earmarking of ADAP funds or to support other means to insure the completion of the St. Thomas Airport project.

Now, of paramount concern to us in this entire initiative, Mr. Chairman, is the survival of our rum industry. In an attempt to offset the obvious threat to both Puerto Rico and the Virgin Islands industries, the legislation proposes to transfer the excise taxes on rum imported from beneficiary Caribbean countries to the Virgin Islands and Puerto Rico.

While the Virgin Islands accepts the excise tax transfer as compensatory, we do not want to lose our rum industry. It means jobs and revenues which are tied to a concrete local produce. We do not want to trade these for a compensatory revenue transfer the basis for which will be increasingly abstract once our industry disappears.

Ideally I would like to see rum, like textiles, excluded from the act. I believe, however, that a compromise is more realistic. The immediate and complete elimination of the present tariff on Caribbean Basin rum from its present level of $1.62 represents a double-barrel threat in the Virgin Islands. It threatens the economic viability of the rum industry as well as the fiscal stability of the territorial government.

Allow me to cite some statistics highlighting the importance of the rum industries to the Virgin Islands and explain how provisions of the proposed legislation fail to adequately protect such a vital sector of this economy. Excise taxes collected on Virgin Islands rum sold on the mainland and rebated to the territory's treasury amounted to $36.2 million in 1980, or approximately 18 percent of all government revenues that year.

It is our largest single source of government revenues. In addition, the rum industry employs approximately 3 percent of our total manufacturing workforce.

In recognition of the importance of this industry and because molasses are not presently produced on the island, the government of the Virgin Islands annually contributes $2 million to assist in the purchase of molasses on terms similar to foreign Caribbean rum producers.

I simply cannot overemphasize the critical significance of the rum industry to the economic well-being of the U.S. citizens in the Virgin Islands.

Why will the elimination of the tariff endanger the rum industry? Eighty-five percent of all Virgin Islands rum consumed on the mainland is unaged rum shipped in bulk. This rum, which is purchased, bottled and sold under private labels, is priced at the lower end of the price scale, thereby making it extremely price sensitive. Once the $1.62 per proof tariff is reduced, foreign rum imports, of which 85 percent presently originate from Caribbean Basin countries, will become cheaper than our own rum and will therefore replace it.

The purchasers of bulk, unaged rum, conscious of their bottom line, will use the least expensive rum for their private labels, and you can be sure that that will not be Virgin Islands rum. Foreign rum producers in the Caribbean already enjoy considerable economic advantages which are not available to our own rum producers. They are not subject to our minimum wage standards or occupational safety and health standards or environmental standards.

They have access to low cost molasses and can ship on lower cost foreign flag bottoms.

Of even greater importance is the fact that pursuant to protocol No. 7 of the Lome Convention of 1975, those Caribbean rum producers can export their product into the European Economic Community and Canada duty free, subject to certain quotas, while Virgin Islands rum is effectively prevented from competing in those markets because of the high tariff.

Allowing foreign Caribbean rums to have duty free access into the U.S. market in addition to their duty free access to European and Canadian markets without similar access for Virgin Islands rum producers is not a fair exchange and would limit our industry's ability to compete on the world markets.

In fact, such a situation coupled with the lower production cost of foreign rum producers resulting from the reasons already set forth and stated, and which you are very sensitive to because of what is happening in your districts, will certainly assure foreign rum producers with a competitive advantage which will most probably destroy our own industry.

Furthermore, most of the rum producers operating on the Virgin Islands and Puerto Rico are multinational companies which also own and operate underutilized distilleries elsewhere in the Caribbean. All they have to do is transfer production in the Virgin Islands and Puerto Rico to their foreign facilities so that no new distilleries may even be built.

Clearly, the minimal regulatory burden, together with the duty free access to foreign and U.S. markets, would give foreign rum producers an unsurmountable competitive advantage over our own rum producers.

Thus, in addition to the excise tax provisions, I urge this subcommittee to amend the act to provide the following: One, require negotiation of agreements permitting Virgin Islands and Puerto Rican rum to gain access to European markets along with other Caribbean states which presently enjoy such tariff preferences.

Two, have a progressive quota system to allow for orderly growth in duty-free imports. My statement spells this out, but I do want to stress that this formula, this quota in no way inhibits the immediate extension of tariff exemptions to rum produced in the CBI companies.

As regards the excise taxes to be transferred to the Virgin Islands and Puerto Rico, I ask the subcommittee to make the language more specific since the Virgin Islands is in greater jeopardy due to its sale in bulk, of unaged rum as opposed to Puerto Rico's brand name sales of aged rum.

The act should specify the President will turn over a set amount based on 1981 sales to compensate the Virgin Islands for losses to other Caribbean distillers. Any excise tax over that amount should be divided between the Virgin Islands and Puerto Rico, with no less than 25 percent to the Virgin Islands. This formula should be specified in the act.

In addition, EPA costly waste-water treatment requirements totally inappropriate to our rum facility must be dropped. I realize that this matter falls under another committee's jurisdiction, and I will pursue that before the appropriate committee.

With these provisions, we believe that our rum industry could survive duty-free rum imports from other Caribbean countries.

Part of our negotiations with the administration not reflected in the legislation is support for a bill that I have introduced, H.R. 5113, which is currently in the Ways and Means Committee. This bill is designed to make the Virgin Islands more competitive with its Caribbean neighbors by reducing the 30 percent tax withheld on passive income such as interest and dividends to 10 percent. This 30 percent tax has inhibited business investment in the Virgin Islands since the tax is viewed as punitive.

I would ask this committee and the administration to support this legislation, particularly in view of the Caribbean Basin Initiative.

Another area of concern to the Virgin Islands is the demise of our watch industry, which has gone from employing 1,300 persons and adding over $100 million in wages and taxes to the Virgin Islands economy since its inception to employment of less than 300 persons in the last 2 years.

To save our watch industry, I introduced H.R. 5738. The bill eliminates the present requirement that at least 30 percent of the value be added in the Virgin Islands. This precludes our industry from competing with the low tariff schedules for watch parts entering the U.S. mainland. My bill also adds production incentives designed to reward labor-intensive watch companies.

I consider support of this fairly innocuous bill to save one of our existing industries a small concession in light of the Caribbean Basin plan, which threatens to inhibit new industry in the U.S. territories.

I have some additional concerns in regard to the 75/25 rule. First of all, I appreciate the inclusion of the Virgin Islands and Puerto Rico as beneficiary countries. In addition, I urge a minor amendment to the provision requiring goods from beneficiary countries to go directly to the United States in order to be eligible for duty-free treatment.

The amendment would allow these goods to go through the Virgin Islands without losing their duty-free status. It would not be necessary for Puerto Rico since it is already within the U.S. customs law. This would be consistent with the twin plant concept, which would allow the Virgin Islands and Puerto Rico to provide the skilled labor add-ons to Caribbean Basin products.

In this context I do want to say I appreciate the endorsement of my legislation currently before the subcommittee which would raise the foreign content permitted from 50 percent to 70 percent. I also appreciate the language in the act allowing the Virgin Islands and Puerto Rico to receive treatment equal to that of beneficiary countries under the 75/25 test, if preferable.

Again, I point out that given our position as offshore areas subject to U.S. laws, this could still leave us at a considerable competitive disadvantage.

In closing I want to make clear that the Virgin Islands stands ready to play its role along with Puerto Rico as the part of the country most able through our cultural affinity to link U.S. interest in the Caribbean with the needs of our neighbors. We are pleased to see that the administration supports development of the

Eastern Caribbean Center at the College of the Virgin Islands and note its plans to use the Virgin Islands and Puerto Rico for agricultural training and assistance programs.

My hope is that a program by the United States to help our Caribbean neighbors will contain sufficient safeguards to assure the protection of U.S. citizens living in its territories.

The amendments I have proposed today will make the Caribbean Basin legislation do just that.

Mr. Chairman, I thank you for your attention. If there are any questions, I would be glad to answer them now.

[The prepared statement follows:]

STATEMENT OF HON. RON DE LUGO, VIRGIN ISLANDS DELEGATE

Mr. Chairman, members of the subcommittee, Governor Luis of the Virgin Islands and myself are here today to testify regarding our concerns about the Presidents proposed Caribbean Basin Initiative.

I recognize that the Committee has placed the Caribbean Basin Economic Recovery Act on a fast track in order to accommodate the President's desire to aid the region in as short an order as possible. I agree that it is important for us to focus attention on assisting our economically depressed, and subsequently politically volatile, neighbors. There are, however, some real concerns as to the effect this Act will have on the U.S. flag terriories in the Caribbean.

In his message to Congress last Wednesday, the President stated, and I quote:

"Puerto Rico and the U.S. Virgin Islands have a longstanding special relationship with the United States. Their development must be enhanced by our policy toward the rest of the region. We have consulted closely with Puerto Rico and the Virgin Islands about the Caribbean Basin Initiative and the legislation I am requesting today will reflect Puerto Rican and Virgin Island interest in many important ways."

I think it is great that the President has said the U.S. Virgin Islands and Puerto Rico must be "enhanced" by the policy toward the Caribbean Basin.

Let's be realistic. No one looking at this legislation can say that the position of the flag territories is enhanced. Yet, the fact is we are not that far from a compromise position which would allow us in the U.S. territories to survive a Caribbean Initiative.

For the flag territories to survive this initiative, certain safeguards and additional incentives are imperative. Some of these safeguards and incentives have been incorporated in the Act. Extension of the Accelerated Cost Recovery System (A.C.R.S.) and Investment Tax Credit (I.T.C.) to companies operating in the flag terriories, along with the direct investment and pass through provisions will help offset the impact of extending the ITC benefits to Caribbean Basin countries.

One Safeguard which we stressed as a priority from the beginning of our negotiations with the Administration, is completion of the St. Thomas, Virgin Islands airport. This airport has repeatedly been at the top of the black star airport list, one of the most dangerous airports in the world. This, coupled with the fact that there are only two airports in the Caribbean region smaller than St. Thomas', places us at a clear disadvantage in an area where access by air determines the success of tourism as well as other business development.

In the fact sheet on the President's OAS speech, announcing his Caribbean Policy, it was clearly stated that,

". . . legislation under the Caribbean Basin Initiative will reflect Puerto Rican and Virgin Islands interests in the following ways:

". . . Expansion of airports in the Virgin Islands and other measures to encourage the developement of Puerto Rico and the Virgin Islands as a transportation hub for the Caribbean region."

Once the ADAP bill moves out of the Ways and Means Committee, we will expect the Secretary of Transportation to honor his commitment to us to support the earmarking of ADAP funds or to support other means to insure the completion of the St. Thomas airport project.

Of paramount concern to us in this entire initiative is the survival of our rum industry. In an attempt to offset the obvious threat to both the Puerto Rico and Virgin Islands industries, the legislation proposes to transfer the excise taxes on rum imported from beneficiary Caribbean countries to the Virgin Islands and Puerto Rico. While the Virgin Islands accepts the excise tax transfer as compensatory, we do not want to lose our rum industry. The industry means jobs and it means revenues which are tied to a concrete local produce. We do not want to trade these for a compensatory revenue transfer, the basis for which will be increasingly abstract once our industry disappears.

Ideally I would like rum, like textiles, excluded from the Act. I believe, however, that a compromise is more realistic. Thus, in addition to the excise transfer provisions, I urge the Subcommittee to amend the Act to provide the following: (1) require negotiations of agreements permitting Virgin Island rums to gain access to European markets along with other Caribbean states which presently enjoy such tariff preferences; and (2) have a progressive quota system to allow for orderly growth in duty free imports.

The immediate and complete elimination of the present tariff on Caribbean Basin rum from its present level of $1.62 per proof gallon represents a double-barreled threat to the Virgin Islands: it threatens the economic viability of the rum industry as well as the fiscal stability of the territorial government. Allow me to cite some statistics highlighting the importance of the rum industry to the Virgin Islands and to explain how the provisions of the proposed legislation fail to adequately protect such a vital sector of our economy.

Excise taxes collected on Virgin Island rum sold on the mainland and rebated to the territory's treasury amounted to $36.2 million in 1980, or approximately 18 percent of all government revenues that year. It is our largest single source of government revenue. In addition, the rum industry employs approximately 3 percent of our total manufacturing workforce. In recognition of the importance of this industry and because molasses are not presently produced on the island, the government of the Virgin Islands annually contributes $2 million to assist in the purchase of molasses on terms similar to foreign Caribbean rum producers. I simply cannot over emphasize the critical significance of the rum industry to the economic well-being of the Virgin Island.

Why will the elimination of the tariff endanger the rum industry? Eighty-five percent of all Virgin Island rum consumed on the mainland is unaged rum shipped in bulk. This rum, which is purchased, bottled and sold under private labels, is priced at the lower end of the price scale thereby making it extremely price sensitive. Once the $1.62 per proof gallon tariff is reduced, foreign rum imports, of which 85 percent presently originate from Caribbean Basin countries, will become cheaper than our own rum and will therefore replace it. The purchasers of bulk unaged rum, conscious of their bottom line will use the least expensive rum for their private labels—and you can be sure that it will not be Virgin Island rum.

Foreign rum producers in the Caribbean already enjoy considerable economic advantages which are not available to our own rum producers. They are not subject to our minimum wage standards, to our occupational safety and health standards, to our environmental standards; they have access to low cost molasses and can ship on lower cost foreign flag bottoms. Of even greater importance is the fact that pursuant to Protocol No. 7 of the Lome Convention of 1975, those Caribbean rum producers can export their product into the European Economic Community and Canada duty-free, subject to certain quotas, while Virgin Island rum is effectively prevented from competing in those markets because of the high tariff. Allowing foreign Caribbean rums to have duty-free access into European and Canadian markets without similar access for Virgin Islands rum producers is not a fair exchange and would limit our industry's ability to compete on the world markets. In fact, such a situation, coupled with the lower production costs of foreign rum producers resulting from the reasons already set forth, will certainly assure foreign rum producers with a competitive advantage which will most probably destroy our own industry. Furthermore, most of the rum producers operating on the Virgin Islands and Puerto Rico are multinational companies which also own and operate underutilized distilleries elsewhere in the Caribbean. All they have to do is transfer production from the Virgin Islands and Puerto Rico to their foreign facilities so that no new distilleries may even be built. Clearly the minimal regulatory burden together with the duty free access to foreign and United States markets would give foreign rum producers an unsurmountable competitive advantage over our own rum producers.

I believe that there are ways to further the expressed intent of the Caribbean Basin Initiative without placing in jeopardy the rum industry which is so vital to the Virgin Islands. One such way would be to provide for an orderly growth in the importation of duty free rums through the use of progressively higher quotas. As has been proposed in the case of sugar imports, the President, in furtherance of this nation's foreign policy interests, should establish an annual duty free quota for particular Caribbean Basin countries. These individual quotas, which could begin with an amount equal to last year's imports into the United States, could be increased by 10 percent annual increments. Amounts imported into the United States which exceed the quota would be subject to the applicable tariff on foreign rum for that year. The quotas would remain available and would continue to expand annually only if the following two conditions were satisfied each year:

(1) Total exports of Virgin Islands' rum to the United States, exceeded 95 percent of their 1981 base year levels; and (2) Virgin Islands' rum exports had access to markets in Canada, the European Economic Community, and Caribbean Basin Initiative partners on terms and conditions at least equal to those available to the rum exported from the particular country seeking a duty-free quota from the United States.

I believe that this proposal represents fair compromise. It assures that our Caribbean neighbors will be able to share on a duty-free basis any expansion in the overall rum market while insuring that the Virgin Island's rum industry will not be destroyed.

I further believe that as an integral part of the Caribbean Basin Initiative, the Congress should reduce the competitive disadvantages of industry located in the Virgin Islands and Puerto Rico by removing unnecessary regulatory burdens which should not be applicable because of the particular geographic or environmental condition of these islands. This is particularly true with the Virgin Islands rum industry. The Environmental Protection Agency has required the construction of a $4 million waste treatment plant to treat effluents which are presently discharged and dissipated into the Caribbean Sea, although there is no clear proof that such effluents are harmful to marine life. The cost of such a plant could exceed the book value of the present rum distillery's facilities. Clearly, such regulatory burden contributes to the cost of Virgin Islands' rum at the expense of its competitive position, because foreign producers do not have to bear such a burden.

I am concerned that Title II of the Trade Act does not provide sufficient safeguards for Virgin Islands industries, particularly its rum industry. Title II provides an ex post facto remedy to harm which our industries could not absorb. I, therefore, request that the law be liberalized to trigger action under Title II more effectively.

Let me briefly address some other issues relating to our rum industry which arise out of provisions of the proposed legislation. Subsection 104(b) of the bill does not provide for mandatory "shapback" of tariffs in the event of a reduction in excise taxes covered into the Virgin Island treasury. Because of the essential nature of these revenues to our government, any reduction in such revenues should automatically trigger the reinstitution of the tariff on foreign rums. Therefore, I strongly recommend that the "snapback" provisions be made mandatory upon the reduction in rum excise taxes being covered into the Virgin Islands treasury.

Similarly, Sect. 302 does not provide that the Virgin Islands shall receive a share of all excise taxes collected on foreign imported rums. It provides that all such excise taxes shall be covered into the Virgin Islands and Puerto Rico treasuries only if the amount per proof gallon on foreign rums paid over does not exceed the amount per proof gallon on Virgin Island or Pureto Rican rum paid ofver to the treasuries of those territories. Clearly, if the excise tax on foreign rums were to be raised, or if the excise tax on Virgin Island and Puerto Rican rums were to be lowered so that a differential would result in a higher excise tax on foreign rums, then the amount of excise taxes collected pursuant to such a differential would not have to be covered into the treasuries of the possessions. I believe that there is no basis for such a distinction.

Finally, I should like to point out that Section 302 docs not provide the Secretary of the Treasury with any guidelines for establishing the formula for allocating between the Virgin Islands and Puerto Rico any excise taxes collected on foreign rums. Given the precarious economic situation of our rum industry relative to that of Puerto Rico which presently controls 87 percent of the domestic rum market, I should like to offer the following formula for allocating such excise taxes:

(1) In distributing any excise taxes collected on foreign rums imported into the United States the amount of such taxes shall first be made available to the Virgin Islands to make up the taxes collected on sales of Virgin Island rums in the United States and the amount of such excise taxes covered onto the treasury of the Virgin Islands in fiscal year 1981; and

(2) Any amount remaining shall then be distributed between the Virgin Islands and Puerto Rico in proportion to their sales of rum on the United States market; provided, however, that the Virgin Islands shall in no event receive less than 25 percent of any remaining funds.

This formula will enable the Virgin Islands to provide our rum industry with additional resources with which to assist it in competing with their stronger rivals throughout the Caribbean.

In summary, the Virgin Islands is willing to share with its neighbors an expanding domestic rum market as part of our contributon to the goals of the Caribbean Basin Initiative; but we are willing to do so in an orderly manner which will not jeopardize one of our few viable industries, and one which is so important to the fiscal and employment situation of the territory.

With these provisions, we believe our rum industry could survive duty-free rum import from other Caribbean countries.

Part of our negotiations with the Administration, not reflected in the legislation, is support for a bill I have introduced, H.R. 5113, which is currently in the Ways and Means Committee. The bill is designed to make the Virgin Islands more competitive with its Caribbean neighbors by reducing the 30 percent tax withheld on passive income, such as interest and dividends, to 10 percent. This 30 percent tax has inhibited business investment in the Virgin Islands, since the tax is viewed as punitive. I would ask this Committee and the Administration to support this legislation, particularly in view of the CBI.

Another area of concern to the Virgin Islands is the demise of our watch industry. The industry has gone from employing 1,300 persons add-over $100 million in wages and taxes to the Virgin Islands economy, to employment of less than 300 persons in the last two years.

To save our watch industry, I introduced H.R. 5738. The bill eliminates the present requirement that at least 30 percent of the value be added in the Virgin Islands, which precludes our industry from competing with the low tariff schedules for watch parts. My bill also adds production incentives designed to reward labor intensive watch companies.

I consider support of this fairly innocuous bill to save one of our existing industries a small concession in light of the Caribbean Basin plan which threatens to inhibit new industry in the territory.

Furthermore, in view of the 25 percent local content rules of origin test proposed for beneficiary countries, I question whether my bill sufficiently protects our watch industry. Possibly, given the difficulties of the past, a limited exclusion may be necessary for products of beneficiary countries which utilize materials from Column II nations.

I have some additional concerns with regard to the 75/25 rules of origin test. First of all let me say that I appreciate inclusion of the Virgin Islands and Puerto Rico as beneficiary countries for purposes of the 25 percent local content rule. In addition, I urge a minor amendment to the provision requiring goods from beneficiary countries to go directly to the United States in order to be eligible for duty-free treatment. The amendment would allow these goods to go through the Virgin Islands without losing their duty-free status. This would be consistent with the twin plant concept which would allow the Virgin Islands and Puerto Rico to provide the skilled labor add-ons to Caribbean Basin products.

In this context, I do want to say that I appreciate the endorsement of my legislation, currently before the Subcommittee, which would raise the foreign content permitted from 50 percent to 70 percent. I also appreciate the language in the Act allowing the Virgin Islands and Puerto Rico to receive treatment equal to that of beneficiary countries under the 75/27 test, if preferable. Again, I point out that, given our position as offshore areas subject to U.S. laws, this could still leave us at a competitive disadvantage.

In closing I want to make clear that the Virgin Islands stands ready to play its role, along with Puerto Rico, as the part of this country most able, through our cultural affinity, to link U.S. interests in the Caribbean with the needs of our neighbors. We are pleased to see that the Administration supports development of the Eastern Caribbean Center at the College of the Virgin Islands, and note its plans to use the Virgin Islands and Puerto Rico for agricultural training and assistance programs.

My hope is that a program by the United States to help our Caribbean neighbors will contain sufficient safeguards to assure the protection of U.S. citizens living in its territories. The amendments I have proposed today will make the Caribbean Basin legislation do that.

Chairman **GIBBONS**. Why don't you introduce the Governor, and then we will have questions for both of you.

Mr. **DE LUGO**. It is my pleasure to introduce the Governor of the Virgin Islands. We have worked very closely together on the Caribbean Basin Initiative. The Governor has been extremely concerned about the impact of this initiative on the U.S. territory which he governs, and at this time it is my pleasure to introduce to this committee our Governor, Governor Juan Luis.

STATEMENT OF HON. JUAN LUIS, GOVERNOR, U.S. VIRGIN ISLANDS, ACCOMPANIED BY LEROY A. QUINN AND WILLIAM BLUM

Governor LUIS. Thank you, Congressman de Lugo.

Mr. Chairman, distinguished members of this subcommittee, I appreciate very much this opportunity to appear before your committee to present the views of the U.S. Virgin Islands regarding the President's Caribbean Basin Initiative plan.

We have taken advantage of the opportunities given us by the administration to present our views as to what policies and programs should be included in the CBI to benefit the U.S. Virgin Islands.

In our meetings with U.S. Trade Representative William Brock, Ambassador Robert Ryan of the State Department and other administration officials, we have consistently emphasized that the CBI should contain measures which will maintain and improve the ability of the U.S. Virgin Islands to develop its own economy and thus continue to serve as an example to other countries in the region of the political and social stability and the economic advantages that a democratic system such as that in the Virgin Islands can provide.

We pointed out that while the Virgin Islands wishes to insure that the CBI will improve general economic conditions in the entire region, the program should also be structured to avoid damage to our already strained local economy now bearing the severe impact of current Federal budget and tax cuts which are projected to cause a sizable budget deficit this year in the Virgin Islands.

As this committee is well aware, U.S. policy toward its territories has long been based on providing special tax and trade concessions in order that they could develop needed public infrastructure and capital improvements to move toward obtaining self-sustaining economies.

In talking with the administration about its plan for the CBI, we emphasized that the value of the special treatment currently available to U.S. citizens and businesses in the Virgin Islands should not be reduced or eliminated by the granting of similar concessions to foreign nations without compensatory programs designed to generate increased economic activity in the U.S. Virgin Islands.

This is particularly important when one considers that our neighboring Caribbean Islands are more competitive because they do not have to comply with federally imposed regulatory requirements related to environmental protection, fair labor standards, and occupational standard and health, among others, which significantly increase the cost of doing business and investing in the Virgin Islands.

The people of the Virgin Islands welcome and favor the Caribbean Basin Initiative as a recognition by the U.S. Government of the importance of our region, and we understand the necessity for changing foreign policy to promote and strengthen democracy in the Caribbean nations; but we want to emphasize that in some cases the impact of U.S. foreign and domestic policy is shouldered disproportionately by the U.S. territories. In such cases appropriate compensatory Federal action is needed to offset these adverse impacts.

Now that the Caribbean Basin Initiative is before Congress for its careful consideration, we stand ready to work with this committee and the entire Congress to devise new strategies, new opportunities, and new means to permit the territory to continue to grow and prosper in an economically revitalized Caribbean.

In this context I would like to now briefly discuss a few aspects of the proposed CBI legislation. I want to be sure this committee is aware exactly what is and what is not contained in it and to suggest various ways in which it could be improved.

The centerpiece of the President's CBI program is a free trade arrangement by which Caribbean Basin products may be imported into the United States free of all customs duties. When I first discussed this aspect of the CBI with the administration, I expressed the territory's strong opposition to this plan as it applies to various products, and most particularly rum.

As the committee is aware, the United States returns to the Virgin Islands Treasury all of the Federal excise taxes imposed on U.S. Virgin Islands-produced rum that is sold in the United States. In fiscal year 1981 this accounted for $37.1 million, or approximately 15 percent of the territory's budget. For fiscal year 1982, we project this amount to be approximately $40 million.

The Virgin Islands rum industry also provides 3 percent of total local manufacturing employment. I feared then, as I do today, that permitting duty-free access to competing Caribbean rums will destroy our rum industry and the jobs and revenues it provides.

Our rum industry is much more vulnerable to competition from other Caribbean rums than is the Puerto Rican rum industry. About 80 percent of U.S. Virgin Islands rum is sold in bulk and bottled under private labels, used in foods or premixed drinks. Thus, unlike the market for the well-known brands manufactured in Puerto Rico, once the duty is eliminated, the market for U.S. Virgin Islands rum could easily be usurped by distilleries from other countries which can use low cost labor and which are not subject to U.S. environmental and regulatory laws.

Three safeguards relating to rum have been included in the legislation. While they provide some protection for Virgin Islands Government revenues, they provide virtually no protection for the existing production of our rum industry and they do not accommodate the possibility that this industry could otherwise grow and prosper.

The safeguards include the return of excise taxes on foreign rums to the Virgin Islands and Puerto Rico, permitting Virgin Islands industries to petition the International Trade Commission for import relief for injuries caused by increased imports from Caribbean Basin countries, and a so-called snap-back provision which permits the President to withdraw duty-free treatment on rum.

If excise tax revenues returned to the territory are reduced because of the prime importance placed by the President on providing duty-free treatment for rums of Caribbean Basin countries, the

Virgin Islands would be inclined to lend its support to this part of the CPI program, but the territory will not be in a position to do so unless additional safeguard provisions are provided and unless the existing ones are significantly strengthened and clarified.

First, the formula for dividing foreign rum excise revenues between the Virgin Islands and Puerto Rico must be spelled out in the legislation and not left for the determination of the Secretary of the Treasury. We believe that the formula should take account of the fact that the Virgin Islands stands to lose more than Puerto Rico because our rum is sold mostly in bulk.

Congressman de Lugo's testimony describes a formula which I support so long as revenues transferred to the territory are maintained at the minimum level of $40 million during the first year the free trade area is in effect to compensate the possible closing of our rum industry, to compensate for growth that could otherwise be expected to occur. This minimum would be increased by $1 million per year.

We stand ready to work with this committee, the administration and Puerto Rico in devising the final version of this formula.

Second, the snap-back provision must be strengthened to make the withdrawal of duty-free treatment mandatory and not permissive if excise tax revenues are reduced.

Third, our rum industry must be exempted from the EPA requirement to construct an effluent treatment facility at the cost of $5 million to $7 million. This would relieve the distiller from making a burdensome capital investment given the uncertain future of the Virgin Islands rum industry in the context of the Caribbean free trade area.

Fourth, a quota system should be imposed on foreign rums which would phase in duty free treatment over several years but only if it could be shown that Virgin Islands rum production has not suffered a significant decrease attributable to duty-free treatment of foreign rums.

Fifth, ambiguous provisions contained in the proposed legislation limiting the amount of foreign excise taxes to be returned to the territory based on the per unit taxes on Virgin Islands rum as compared to foreign rum must be removed.

Finally, alternative revenue measures must be included in the CBI package so that the territory can become less reliant on what could become under the free trade area proposal a much less reliable source of revenue for the territory. Shortly I will discuss some proposals in this regard.

Absent the six safeguards I have just mentioned, I strongly support exclusion of rum from the free trade area concept for a minimum of at least 5 years. Our concerns about those portions of the CBI legislation relating to the free trade area extend beyond the important rum issue.

For example, under the President's proposal in determining the value added in Caribbean countries under the rules of origin test, U.S. Virgin Islands products and material may be included. In order to stimulate trade between the territory and Caribbean nations, we believe that the legislation also should contain language which would permit Caribbean Basin products to be excluded in determining the foreign content of U.S. Virgin Islands products under headnote 3(a).

That same provision as it is presently drafted is harmful to the Virgin Islands because it reduces from the 35 percent GATT level to 25 percent the value to be added in Caribbean countries. The 25 percent value added test will reduce the Virgin Islands' competitive advantage in the Caribbean.

A liberalization of the headnote 3(a) requirements on watches, as has been proposed by Delegate de Lugo in H.R. 5758, a bill which was developed through the Department of Commerce, would serve to help reduce the negative impact of the value added provision by maintaining a needed competitive edge for the Virgin Islands watch industry.

A provision to permit an increase in the foreign content limitation on nonwatch products from 50 percent to 70 percent has not specifically been included in the administration's CBI legislation, although the President announced last week that the administration would support legislation which would do so.

We urge this committe's support of H.R. 5758 and of the proposed change in headnote 3(a).

A second provision requires that duty-free treatment for Caribbean Basin products will only be available if they are imported directly from a beneficiary country into the U.S. customs territory. A simple amendment to this provision to permit duty-free entry into the United States if the product is imported via the Virgin Islands would prove of great benefit to our tourist-oriented local retail industry and also encourage increased trade between the Virgin Islands and its Caribbean neighbors.

Third, the provision of the CBI legislation extending the protection from increased imports available under section 201 of the Trade Act of 1974 would also expand to the Virgin Islands other helpful provisions of the Trade Act relating to antidumping and countervailing duties.

Also, the CBI legislation would allow tourists to return to the United States from the U.S. Virgin Islands with an additional liter of locally produced alcoholic beverages duty free. We urge this committee's support of this provision, which will prove of some benefit to both our tourist and the rum industries.

In addition to the trade measures with which this committee is primarily concerned, the CBI legislation includes certain tax measures, revenue measures and other measures to promote the economic development of the Caribbean region. I would now like to discuss them briefly.

In the area of taxes, the CBI legislation contains a provision to permit U.S. domestic corporations to receive the benefits of the investment tax credit and the accelerated cost recovery system for investments made in the Virgin Islands and Puerto Rico. At the same time, the legislation would provide for the investment tax credit to be available to other countries in the Caribbean region.

This comparative advantage for U.S. territories is exactly the type of concept that the Virgin Islands needs and supports, and we urge that it be extended to other portions of the legislation as well. Although investment tax credits and accelerated depreciation are useful in attracting capital-intensive industries, our studies have shown that lighter, more labor-intensive industries are the types most likely to invest in the Virgin Islands.

To facilitate such investment, we urge congressional support for H.R. 5113 introduced by Delegate de Lugo at my request, which would lower to 10 percent from 30 percent the tax rate on dividends, interest, and other passive income flowing from the Virgin Islands to the United States and which would remove foreign tax credit restrictions as they relate to this tax.

Such a measure will put the Virgin Islands on a par with the many countries that have negotiated tax treaties with the United States.

We also urge that the CBI legislation be amended to permit the Virgin Islands to participate in U.S. bilateral investment treaties. Other strong measures are needed to stimulate investment and increase trade in the Virgin Islands.

We share many of the same economic development problems with the rest of the Caribbean region. Like our Caribbean neighbors, the Virgin Islands must share in the emergency economic assistance being offered in the Caribbean Basin Initiative legislation, particularly at a time when domestic economic development programs have been reduced and eliminated.

The Federal Government should provide funding for upgrading of power generation and water production, distribution and storage facilities in the territory and for the establishment of a territory development bank. Such funding could take the form of a grant, or preferably it could be handled by returning to the Virgin Islands the excise taxes imposed by the United States on petroleum products manufactured in the Virgin Islands and shipped to the United States.

The latter method has the additional advantage of providing a long-term funding source for territorial needs without the need for annual appropriations. The proposed territorial development bank would provide a low-interest funding source for improvement and expansion of territorial infrastructure and for private sector growth.

Establishment of such an institution is vital in light of the elimination and cutbacks of such domestic funding sources as the Economic Development Administration, the Small Business Administration, and the Farmers Home Administration. It would put the Virgin Islands on a par with other nations in the region which presently have access to low-interest funds through institutions such as the World Bank and the Inter-American Development Bank.

Ironically, even though many of these institutions are funded in part by the United States, they are not permitted to finance investments in U.S. territories. Without a territorial development bank, we are not competitive and our future economic growth will be seriously restricted.

While the U.S. Virgin Islands has attempted to diversify its economy through promoting manufacturing industries, tourism remains the mainstay of the territory. In view of other nations' assistance to neighboring Caribbean islands efforts to expand their airport facilities, we strongly believe that the CBI presents an excellent opportunity for the United States to keep the Virgin Islands competitive by doing likewise in its own territory.

Phase one of the St. Thomas project, which creates the land on which to construct a new runway, is now nearly complete. We have been working with the administration in obtaining the necessary fiscal year 1982 funding to begin phases two and three, runway and terminal construction. We very much appreciate this commitment to the economic future of the territory; however, further funding of an additional $34 million is needed in fiscal years 1983 and 1984.

The Virgin Islands seek the aid of Congress in earmarking the funds to complete this project in the airport and airway development program legislation.

The St. Croix airport is also in need of modernization and expansion. Lengthening of the runway to 10,000 feet would permit nonstop flights to the west coast and Europe. Completion of both projects would allow wide-body flights to both islands and would help tremendously in our efforts to promote tourism.

We have received assurances from the administration that the proposed Eastern Caribbean Center for Educational, Cultural, Technical and Scientific Interchange at the College of the Virgin Islands will be funded. As the only U.S. English-speaking institution of higher learning in the Caribbean, the College of the Virgin Islands is in an excellent position to provide the training, research, and expertise needed to further the economic, cultural, and social development of the English-speaking nations of the region. We believe that the Eastern Caribbean Center should be funded by Congress and that it is consistent with the CBI goals.

Another project, included in the CBI legislation, which would benefit both the territory and the Caribbean as a whole is increased agricultural research. This proposal should be expanded to include the fishing industry, so that both fishing and agriculture may become more viable in the Virgin Islands.

In closing, I wish to reiterate the Virgin Islands' strong support for Federal measures to help promote economic development of our strategically vital region. But I wish to emphasize that if properly implemented this noble effort—the Caribbean Basin Initiative—will be significantly enhanced by the United States insuring that its own territories are first adequately protected.

In so doing, the United States will be in a better position to encourage social and political stability by promoting its trade and investment policies in the region. I ask this committee and the entire Congress to amend and strengthen the administration's CPI legislation where necessary, particularly by providing compensatory funding and economic measures for the territories.

I stand ready to work with this committee as it considers the measures that are needed to improve the position of the U.S. Virgin Islands as it relates to the Caribbean Basin Initiative.

Thank you very much, Mr. Chairman.

[The prepared statement follows:]

STATEMENT OF HON. JUAN LUIS, GOVERNOR, U.S. VIRGIN ISLANDS

Mr. Chairman, distinguished members of this subcommittee, I very much appreciate this opportunity to appear before your committee to present the views of the

United States Virgin Islands regarding the President's Caribbean Basin Initiative plan (CBI).

I was honored to be invited to be present at the meeting of the Organization of American States last month when President Reagan presented the Caribbean Basin Initiative. I was particularly pleased that the President proposed "special measures" for the U.S. Virgin Islands and Puerto Rico as one of the six points in his Caribbean program. The same week of the President's speech, the National Governors' Association passed a resolution calling on the federal government to recognize that whatever action it takes to aid the nations of the Caribbean may have an impact on U.S. Territories in the region and that no action should be undertaken without carefully weighing the consequences to the U.S. Virgin Islands and Puerto Rico.

We have been given several opportunities by the Administration to present our views as to what policies and programs should be included in the CBI to benefit the United States Virgin Islands. We appreciate these opportunities. I believe they affirm the spirit of cooperation, communication, and compromise which consistently have characterized our dealings with the Administration on the development of the Caribbean Basin Initiative.

In order to ensure that the U.S. Virgin Islands input would represent the views of the entire Territory, I appointed a local task force, composed of members of both the public and private sectors, to develop background and position papers for presentation to the Office of the U.S. Trade Representative. The input of this group is also reflected in my remarks of today and I hope you will have an opportunity later in these hearings to hear directly from some of the members of the task force who have accompanied me to Washington.

In our meetings with U.S. Trade Representative William Brock, Ambassador Robert Ryan of the State Department, and other administration officials, we have consistently emphasized that the CBI should contain measures which will maintain and improve the ability of the United States Virgin Islands to develop its economy and thus continue to serve as an example to other countries in the region of the political and social stability and the economic advantages that a democratic system such as that in the Virgin Islands, can provide. We pointed out that while the Virgin Islands wishes to ensure that the CBI will improve general economic conditions in the entire region the program should also be structured to avoid damage to our already strained local economy, now bearing the severe impact of current federal budget and tax cuts, which are projected to cause a harmful budget deficit in the Virgin Islands.

As this committee is well aware, United States policy toward its territories has long been based on providing special tax and trade concessions in order that they could develop needed public infrastructure and capital improvements to move toward obtaining self-sustaining economies. In talking with the Administration about its plans for the CBI we emphasized that the value of the special treatment currently available to U.S. citizens and businesses in the Virgin Islands should not be reduced or eliminated by the granting of similar concessions to foreign nations without compensatory programs designed to generate increased economic activity in the United States Virgin Islands. This is particularly important when one considers that our neighboring Caribbean islands are more competitive because they do not have to comply with federally imposed regulatory requirements relating to environmental protection, fair labor standards, and occupational safety and health, among others, which significantly increase the cost of doing business and investing in the U.S. Virgin Islands. Furthermore, the Virgin Islands unlike its Caribbean neighbors, is not eligible to obtain financial assistance from various international organizations such as the World Bank, the Overseas Private Investment Corporation, and the Caribbean Development Bank.

The people of the Virgin Islands welcome and favor the Caribbean Basin Initiative as a recognition by the U.S. government of the importance of our region, and we understand the necessity for changing foreign policy to promote and strengthen democracy in the Caribbean nations. But we want to emphasize that in some cases the impact of U.S. foreign and domestic policy is shouldered disproportionately by the U.S. territories. In such cases, appropriate compensatory federal action is needed to offset these negative impacts.

Now that the CBI is before Congress for its careful consideration, we stand ready to work with this Committee and the entire Congress, we devise new strategies, new opportunities, and new means to permit the Territory to continue to grow and prosper in an "economically revitalized" Caribbean.

In this context I would like now to briefly discuss a few aspects of the proposed CBI legislation. I want to be sure this Committee is aware exactly what is and what is not contained in it, and to suggest various ways in which it could be improved.

The "centerpiece" of the President's CBI program is a free trade arrangement by which Caribbean Basin products may be imported into the United States free of all customs duties. When I first discussed this aspect of the CBI with the administration I expressed the Territory's strong opposition to this plan as it applies to various products, and most particularly, rum. As the Committee is aware, the United States returns to the Virgin Islands treasury all of the federal excise taxes imposed on U.S. Virgin Islands produced rum that is sold in the United States. In fiscal year 1981 this accounted for $37.1 million or approximately 15 percent of the Territory's budget. The Virgin Islands rum industry also provides three percent of total local manufacturing employment. I feared then, as I do today, that permitting duty free access to competing Caribbean rums will destroy our rum industry and the jobs and revenues it provides.

Our rum industry is much more vulnerable to competition from other Caribbean rums than is the Puerto Rican rum industry. About 80 percent of U.S. Virgin Islands rum is sold in bulk and bottled under private labels or used in foods or premixed drinks. Thus, unlike the market for the well-known brands manufactured in Puerto Rico, once the duty is eliminated the market for U.S. Virgin Islands rum could easily be usurped by distilleries from other countries which can use low cost labor and which are not subject to U.S. environmental and regulatory laws.

Three "safeguards" relating to rum have been included in the legislation. While they provide some protection for Virgin Islands government revenues, they provide virtually no protection for the existing production of our rum industry and they do not accommodate the possibility that this industry could otherwise grow and prosper. The safeguards are as follows: First, excise taxes on foreign rums would be returned to the Virgin Islands and Puerto Rico and divided between the Territory and the Commonwealth according to a formula which has yet to be determined; second, U.S. Virgin Islands industries would be allowed to petition the International Trade Commission under the Trade Act of 1974 for import relief for injuries caused by increased imports from Caribbean Basin countries; and third, by a so-called "snap-back" provision, the President may withdraw duty free treatment on rum if he determines that excise tax revenues returned to the Virgin Islands and Puerto Rico are reduced below the amount that would have been returned if the imported rums had been manufactured in the U.S. Virgin Islands and Puerto Rico.

Because of the prime importance placed by the President on providing duty free treatment for rums of Caribbean Basin countries, the Virgin Islands would be inclined to lend its support to this part of the CBI program, but the Territory will not be in a position to do so unless additional safeguard provisions are provided and unless the existing ones are significantly strengthened and clarified. First, the formula for dividing foreign rum excise revenues between the U.S. Virgin Islands and Puerto Rico must be spelled out in the legislation and not left for the determination of the Secretary of the Treasury. We believe that the formula should take account of the fact that the Virgin Islands stands to lose more than Puerto Rico because our rum is sold mostly in bulk. The formula should be based on relative production during some historical period, perhaps calendar year 1981. We stand ready to work with the Committee, the administration, and Puerto Rico in determining this formula. Second, the "snap-back" provision must be strengthened to make the withdrawal of duty-free treatment mandatory and not permissive if excise tax revenues are reduced. Third, our rum industry must be exempted from the EPA requirement to construct an effluent treatment facility at the cost of $5–7 million dollars. This would relieve the distiller from making a burdensome capital investment given the uncertain future of the Virgin Islands rum industry in the context of a Caribbean free trade area. Fourth, a quota system should be imposed on foreign rums which would phase-in duty-free treatment over several years but only if it could be shown that Virgin Islands rum production had not suffered a significant decrease attributable to duty-free treatment of foreign rums. Fifth, ambiguous provisions contained in the proposed legislation limiting the amount of foreign excise taxes to be returned to the Territory based on the per-unit taxes on Virgin Islands rum as compared to foreign rum must be removed. Finally, alternative revenue measures must be included in the CBI package so that the Territory can become less reliant on what could become, under the free trade area proposal, a much less reliable source of revenue for the Territory. Shortly I will discuss some proposals in this regard.

Our concerns about those portions of the CBI legislation relating to the free trade area extend beyond the important rum issue. First, under the President's proposal, in determining the value added in Caribbean countries under the rules of origin test, U.S. Virgin Islands products and materials may be included. This will be a minor benefit to the Territory because the U.S. Virgin Islands has virtually no raw materials to offer and it does not produce a significant quantity of intermediate products to be used in manufacturing processes. In order to stimulate trade between the Territory and other Caribbean nations, we believe that the legislation also should contain language which would permit Caribbean Basin products to be excluded in determining the foreign content of U.S. Virgin Islands products under Headnote 3(a).

That same provision, as it is presently drafted, is harmful to the Virgin Islands because it reduces, from the 35 percent GATT level to 25 percent, the value to be added in Caribbean countries. The 25 percent value-added test will reduce the Virgin Islands competitive advantage in the Caribbean. A liberalization of the Headnote 3(a) requirements on watches, as has been proposed by Delegate de Lugo in H.R. 5758, a bill which was developed through the Department of Commerce, would serve to help reduce the negative impact of the value-added provision by maintaining a needed competitive edge for the Virgin Islands watch industry. A provision to permit an increase in the foreign content limitation on non-watch products from 50 to 70 percent has been included in the administration's CBI legislation at the Virgin Islands request. We urge this Committee's support of H.R. 5758 and of the proposed change in Headnote 3(a) in the administration bill.

A second provision requires that duty-free treatment for Caribbean Basin products will only be available if they are "imported directly from a beneficiary country" into the U.S. customs territory. A simple amendment to this provision to permit duty-free entry into the United States if the product is imported via the Virgin Islands, would prove of great benefit to our tourist oriented local retail industry and it would also encourage increased trade between the U.S. Virgin Islands and its Caribbean neighbors.

Third, the provision extending the protection from increased imports available under Section 201 of the Trade Act of 1974 should be expanded to provide additional protections under that Act for U.S. Virgin Islands industries. Extension of the anti-dumping and countervailing duty provisions of the Trade Act to the Virgin Islands would help protect Virgin Islands industries, such as the watch industry, that might be hurt by foreign manufacturers who take unfair advantage of the free-trade area concept.

Also the legislation would allow tourists to return to the United States from the U.S. Virgin Islands with an additional liter of locally produced alcohol beverages duty free. We urge this Committee's support of this provision which will prove of some benefit to both our tourist and rum industries.

In addition to the trade measures with which this committee is primarily concerned, the CBI legislation includes certain tax measures, revenue measures, and other measures to promote the economic development of the Caribbean region. I would now like to discuss them briefly.

In the area of taxes, the CBI legislation contains a provision to permit U.S. domestic corporations to receive the benefits of the Investment Tax Credit and the Accelerated Cost Recovery System for investments made in the U.S. Virgin Islands and Puerto Rico. At the same time, the legislation would provide for the Investment Tax Credit to be available to other countries in the Caribbean region. This comparative advantage for U.S. Territories is exactly the type of concept that the Virgin Islands needs and supports, and we urge that it be extended to other portions of the legislation as well. At the same time, however, there is a distinct need for other tax incentives to be extended to investors in the United States Virgin Islands. While investment tax credits and accelerated depreciation are useful in attracting capital intensive industries, our studies have shown that lighter, more labor intensive industries are the types most likely to invest in the U.S. Virgin Islands. To facilitate such investment we urge Congressional support for H.R. 5113, introduced by Delegate de Lugo at my request, which would lower to 10 from 30 percent the tax rate on dividends, interest, and other passive income flowing from the Virgin Islands to the United States and which would remove foreign tax credit restrictions as they relate to this tax. Such a measure will put the Virgin Islands on a par with the many countries that have negotiated tax treaties with the United States. We also urge that the CBI legislation be amended to permit the Virgin Islands to participate in U.S. bilateral investment treaties.

Other strong measures are needed to stimulate investment and increased trade in the Virgin Islands. We share many of the same economic development problems with the rest of the Caribbean region. Like our Caribbean neighbors, the Virgin Islands must share in the Emergency Economic Assistance being offered in the Caribbean Basin Initiative legislation, particularly at a time when domestic economic development programs have been reduced and eliminated. The federal government should provide funding for upgrading of power generation and water production, distribution, and storage facilities in the Territory and for the establishment of a

Territorial Development Bank. Such funding could take the form of a grant, or, preferably, it could be handled by returning to the Virgin Islands the excise taxes imposed by the United States on petroleum products manufactured in the Virgin Islands and shipped to the United States. The latter method has the additional advantage of providing a long term funding source for Territorial needs without the need for annual appropriations.

The proposed Territorial Development Bank would provide a low-interest funding source for improvement and expansion of territorial infrastructure and for private sector growth. Establishment of such an institution is vital in light of the elimination and cutbacks of such domestic funding sources as the Economic Development Administration, the Small Business Administration, and the Farmers Home Administration. It would put the Virgin Islands on a par with other nations in the region which presently have access to low interest funds through institutions such as the World Bank and the Inter-American Development Bank. Ironically, even though many of these institutions are funded in part by the United States, they are not permitted to finance investments in U.S. Territories. Without a Territorial Development Bank we are not competitive and our future economic growth will be seriously restricted.

While the U.S. Virgin Islands has attempted to diversify its economy through promoting manufacturing industries, tourism remains the mainstay of the Territory. In view of other nations' assistance to neighboring Caribbean Islands' efforts to expand their airport facilities, we strongly believe that the CBI presents an excellent opportunity for the United States to keep the Virgin Islands competitive by doing likewise in its own Territory. In 1976, the federal government agreed to fund an expansion of the St. Thomas airport, rated as a black star airport, by extending its 4800 foot runway into the sea and by leveling two hills which have made the airport only marginally safe for jet operations. Phase I of the project, which creates the landfill on which to construct the new runway, is now nearly complete. We have been working with the administration in obtaining the necessary fiscal year 1982 funding to begin Phases II and III, runway and terminal construction. We very much appreciate this commitment to the economic future of the Territory. However, further funding of an additional $34 million is needed in fiscal years 1983 and 1984. The Virgin Islands seeks the aid of Congress in earmarking the funds to complete this project in the Airport and Airway Development Program legislation.

The St. Croix airport is also in need of modernization and expansion. Lengthening of the runway there to 10,000 feet would permit non-stop flights to the West Coast and to Europe. Completion of both projects would allow wide-body flights to both islands and would help tremendously in our efforts to promote tourism.

We have received assurances from the administration that the proposed Eastern Caribbean Center for Educational, Cultural, Technical, and Scientific interchange at the College of the Virgin Islands will be funded, although no appropriation is included in the CBI legislation. As the only United States, English-speaking institution of higher learning in the Caribbean, the College of the Virgin Islands is in an excellent position to provide the training, research and expertise needed to further the economic, cultural, and social development of the English speaking nations of the region. We believe that the Eastern Caribbean Center should be funded by Congress and that it is consistent with the CBI goals.

Another project, included in the CBI legislation, which would benefit both the Territory and the Caribbean as a whole is increased agricultural research. This proposal should be expanded to include the fishing industry so that both fishing and agriculture may become more viable in the Virgin Islands.

In closing, I wish to reiterate the Virgin Islands' strong support for federal measures to help promote economic development of our strategically vital region. But I wish to emphasize that if properly implemented, this noble effort, the Caribbean Basin Initiative, will be significantly enhanced by the United States ensuring that its own territories are first adequately protected. In so doing the United States will be in a better position to encourage social and political stability by promoting its trade and investment policies in the region. I ask this committee and the entire Congress to amend and strenthen the administration's CBI legislation where necessary, particularly by providing compensatory funding and economic measures for the territories.

I stand ready to work with this Committee as it considers the measures that are needed to improve the position of the United States Virgin Islands as it relates to the Caribbean Basin Initiative.

Thank you very much.

Chairman GIBBONS. Thank you, Governor. And thank you, Mr. de Lugo.

Let me ask some questions, basic questions about the Virgin Islands. First of all, the last time I went there I think was in the 1960's, and I realize that conditions have changed a lot. I think one of the first things you recognize is that the islands are a beautiful place.

But you also recognize what a difficult job it is to make them economically viable in today's setting. And I realize also the necessity for transportation into that area.

What is the population of the Virgin Islands today?

Governor LUIS. The population stands at approximately 100,000.

Chairman GIBBONS. About 100,000. What is the birth rate? Do you happen to know the birth rate increase? Well, I imagine most of the population of the islands has increased by migration, but what is its basic birth rate, do you know?

Governor LUIS. Mr. Chairman, I do not have the birth rate, but you are quite correct that most of the increase in the population of the Virgin Islands has been through migration or immigration, and that has tripled.

Chairman GIBBONS. Let me ask you, I have never been to St. Croix and I realize it is the largest of the islands. It is also the island with the greatest agricultural and industrial base, is that right? Is that where your rum is distilled, in St. Croix?

Governor LUIS. That is correct.

Chairman GIBBONS. And the sugar is grown there, or is it imported?

Governor LUIS. The molasses is imported. We used to grow sugar and this has been abandoned.

Mr. DE LUGO. The Federal Government actually made the decision to go out of the growing of sugar in the Virgin Islands when it was shown to be simply uneconomical and very unreliable because of the rainfall.

Chairman GIBBONS. The rain situation.

Mr. DE LUGO. Right. It was a fairly recent decision. We were in sugar up until the midsixties, and on St. Croix we have agricultural lands. We have the Hess oil refinery, Martin-Marietta aluminum plant, massive industries of that nature.

Chairman GIBBONS. Now, is the bauxite for the aluminum plant mined there on the island or is it imported?

Governor LUIS. It is imported.

Chairman GIBBONS. As I recall, the airport in St. Thomas was classified as the worst commercial airport in the world, and I assume it still is the worst commercial airport in the world that I know of. What progress is taking place—you say you have gotten landfill for the extension of the runway, is that right?

Governor LUIS. We are actually building the runway into the ocean.

Chairman GIBBONS. Yes, I know.

Governor LUIS. And we have prepared—we are now preparing this land, which is almost complete. And in negotiating with the administration we have obtained a commitment for receiving $6 million to complete phase 1, and we have not received any commitment—I am sorry, $6 million to start phases 2 and 3, because we have funding to complete phase 1.

But there is no commitment to complete the airport beyond that, so we would have to lobby for the additional funds. And for that reason we have highlighted this problem before this committee.

Chairman GIBBONS. Mr. de Lugo?

Mr. DE LUGO. I was just going to expand a bit on the airport project. It is an incredible project. I had Chairman Jim Howard of the Public Works Committee down there and several other Members. What the Government of the Virgin Islands is doing is expanding the present runway, which is 4,650 feet, to a 7,000-foot runway.

And you should see this project. They have taken down two mountains. They have been removed. The earth fill will be completed within the next 2 months.

Chairman GIBBONS. You are in pretty deep water.

Mr. DE LUGO. Ninety feet of water. It is an incredible engineering feat. And when that is completed in the next few months, then we move on to phases 2 and 3, which are the terminals and the building of the taxiways.

And this has been a high-priority item for this administration and for previous administrations. We have met, the Governor and myself, with the Secretary of Transportation. We have met over at the White House and received certain assurances, and we are counting on those assurances to see this project through.

Chairman GIBBONS. I assume in order to get to St. Thomas it is still required that you have to fly to Puerto Rico and then transfer to a smaller plane, is that right?

Mr. DE LUGO. There is limited direct service out of Miami, but these are 727's. That is the largest thing that can come in there, and they are not fully loaded. When you land there you are glad they are not fully loaded, and you will wish you were on something else.

Chairman GIBBONS. I have been through that.

Mr. DE LUGO. That is how we got the initial funding. I took some members down and we landed at that airport. And you can believe me, anybody that lands there——

Chairman GIBBONS. The first time I landed there you had to have jet-assisted takeoff bottles hung under the wings, and I prayed pretty hard that time.

Mr. DE LUGO. Originally there was a swamp there, and the airport was built by the Marine Corps prior to World War II. And you know, they used those small biplanes.

Chairman GIBBONS. The problem is there is just no other place for an airport.

Mr. DE LUGO. There is nowhere else. So they are taking down the mountains. We have got them down. It is incredible. It is going to be a fantastic airport once it is completed.

Governor LUIS. Mr. Chairman, on that point, why we have limited direct flights, as Congressman de Lugo has explained, most of the tourists come through Puerto Rico in small planes, and we have found that this discourages the tourist movement.

Chairman GIBBONS. No doubt about that.

Governor LUIS. Because of the many inconveniences that are experienced.

Mr. DE LUGO. I might state also that American Airlines has refused to fly its jets into St. Thomas.

Chairman GIBBONS. Your rum industry is one of your critical concerns. The molasses for it is imported. Therefore, you really enjoy no competitive advantage as far as your neighbor is concerned.

How many plants or distilleries have you got making rum?

Governor LUIS. We have one—no, two, one small one and a large one.

Chairman GIBBONS. And it provides 3 percent of your island's employment; is that right?

Governor LUIS. That is correct, sir, manufacturing employment.

Chairman GIBBONS. Manufacturing employment.

Governor LUIS. Yes.

Chairman GIBBONS. Roughly how many people is that?

Governor LUIS. That is about 100.

Chairman GIBBONS. Your principal problem is you do not think the concessions that are being made are enough, the concessions to the rest of the basin are so strong it would wipe out your rum industry; is that what you feel?

Governor LUIS. That is correct. The rum industry is significant to us because of the return of the excise taxes which for fiscal year 1982 are projected to some $40 million.

Chairman GIBBONS. That is a good return for that island.

Mr. DE LUGO. The problem is, Mr. Chairman, that when we extend all of these benefits to the CBI nations or countries, that we are not competitive because they do not have minimum wages, they do not have OSHA and all these Federal regulations that must be met in the U.S. territory.

Chairman GIBBONS. What is it that EPA wants you to do with that one rum plant down there?

Governor LUIS. They are requiring that an effluent treatment plant be constructed, which would amount to $5 to $7 million. This is a costly project for our rum industry, which is now threatened by CBI. Besides, our studies have shown that for many years what they refer to as the by-product being dumped in the ocean has done no damage.

Mr. DE LUGO. If I may address myself to that. I serve on the Interior Committee and Public Works. I am one of the strongest supporters of environmental legislation. But waste that is dumped into the ocean from the distillery, I do not view that as harmful. And in fact there are those that argue that it actually encourages the breeding of fish. And that is how we view it down in the islands.

It is not causing an unpleasant situation, but EPA—and they have got this under study at the present time, under appeal—is asking for the expenditure of some $6 to $7 million, and that is more than the entire book value of the Schendley plant that is there. So it is a very serious problem.

Chairman GIBBONS. What side of the island is the plant on?

Governor LUIS. The south shore.

Chairman GIBBONS. As I recall, the ocean currents move to the west there. There is nothing for about a thousand miles out that way, is there? That ought to be enough to dissipate most effluent.

Governor LUIS. That is correct, sir.

Mr. de Lugo. This is one of the Federal regulations that does not seem to be applicable to a territory in the middle of the Caribbean that has, as you point out, strong ocean currents involved and trade winds.

Chairman Gibbons. Are there any islands close to the westerly drift?

Governor Luis. No, not really, not to St. Croix.

Chairman Gibbons. St. Croix from there on, it is pretty much open water.

Governor Luis. The rum industry is on St. Croix, and we have no close-by inhabited islands.

Chairman Gibbons. Well, let me ask you about your watch industry—well, for a while I will stay on rum. You had a division of the returned excise tax, that legislation requires the Secretary of the Treasury to come up with some division formula. You say you would rather have that spelled out.

Mr. de Lugo, you mentioned a 75-25 distribution of that revenue. I assume in your discussions with the administration in developing this legislation you must have asked for that. Can you tell us why they turned you down?

Mr. de Lugo. To tell you the truth, we did not ask for that, because we were focusing in on the larger question of quotas, which meant the very survival of the rum industry, and we had not gotten into this question.

Chairman Gibbons. What is the rationale for the 75-25?

Mr. de Lugo. That is an approximate division based on the impact to the present market of Puerto Rico and the Virgin Islands. With all due respect to my good friend, the Resident Commissioner from Puerto Rico, I feel it is a fair division because Puerto Rico has a much stronger rum industry. In fact, they have a very healthy rum industry. They spend some $22 million a year in the promotion of this aged rum, name branded. It is advertised everywhere as Puerto Rican rum by name, and we do not have the resources to do that in the Virgin Islands.

With this sort of division, this would help us to strengthen our rum industry. And there is no question, and I think Puerto Rico would agree and everyone we have spoken to agrees, that the industry in greatest jeopardy by this Caribbean Basin Initiative is the industry in the Virgin Islands, for the simple reason that our rum is unaged, it is sold in bulk, and this is the rum that will also be shipped from the Caribbean Basin Initiative islands. Puerto Rican rum is sold by label, by name, and they have a very strong market that will not be affected that much.

Chairman Gibbons. Now, you mentioned that 30 percent withholding tax and you want to reduce that to 10 to make you competitive with other islands down there with which we have tax treaties. That is the basis of your——

Governor Luis. That is correct.

Chairman Gibbons. That sounds reasonable. I do not know why we have not done it. Can you explain to me why we have not done it? Does the administration oppose that or is it because we have the 30-percent withholding tax up here on the mainland?

Governor Luis. Our experience in attracting industries, whenever they have visited us and they have studied the possibility of coming in, every time they discover the 30-percent withholding tax that is a major deterrent.

Chairman GIBBONS. I would imagine so.

Governor LUIS. That is the one and it is harmful to us. And this is a very good opportunity to have a change. But naturally, we cannot change that tax on our own and we are asking the Congress to do so.

Mr. DE LUGO. Perhaps the reason we did not change it up to now is because if you are getting 30 percent in revenue you figure that is going to help your coffers more than 10 percent. But we found out that the 30 percent simply was discouraging investments.

Chairman GIBBONS. That is the same thing we have here on the mainland; 30 percent is the mainland withholding rate, and we are faced with that emotional problem of, what do you do when you change that. It is not a real problem because we just do not collect it.

Mr. DE LUGO. We are now convinced that lowering it to 10 percent will encourage investment and actually increase our revenues.

Chairman GIBBONS. All right. How about your watch industry? I did not follow through exactly on that. What have you got in mind? What changes do you want so far as the watch industry is concerned?

Mr. DE LUGO. Mr. Chairman, I have with me Margaret Martin of my staff, who has spent considerable time working with the administration on the watch bill.

Ms. MARTIN. Mr. Chairman, what the watch bill does is to take away the tariff requirements.

Chairman GIBBONS. The 30-percent component requirement?

Ms. MARTIN. Right, so that we would have 100-percent foreign content. And then the second part of the bill——

Chairman GIBBONS. It would be 100-percent foreign content?

Ms. MARTIN. The reason is we have had a difficult time competing with the low-tariff watch components that have been coming into the mainland, and that has been a basis for the decline of our watch industry.

The bill also has production incentives——

Chairman GIBBONS. Would you have any—you would just be importing watches and selling them if you didn't have any components, would you not? Would there be any value added at all in the islands?

Ms. MARTIN. The Virgin Islands would still be subject to the minimum assembly test required under present law. In addition, the second part of the bill that has the production incentives, is designed to enhance production in the islands. Based on the wages paid in the islands, these certificates would be given to the local watch companies and the companies could sell the certificates back to mainland watch companies. In this way they would be encouraged to hire people on the islands to work on the watches there.

And the idea of the bill is to do away with the tariff disincentive while on the other hand enhance production in the islands.

Chairman GIBBONS. Did you negotiate with the administration on this proposal?

Ms. **Martin**. Yes; we have. The bill came out of the Commerce Department. We worked with Commerce on the bill and then introduced the bill. And Interior also supports this bill.

Chairman **Gibbons**. Why did they not include it in the Caribbean Initiative?

Ms. **Martin**. We did not want it included because we were hoping to move it more quickly than we thought the initiative would move. We are very concerned about getting this bill through quickly. The watch companies are in jeopardy and we see this as something that has to be taken care of this year.

Mr. **de Lugo**. The problem was also that, while Commerce developed a bill and Interior has endorsed it, it has not gone through the process of being endorsed by all of the various departments and agencies in the administration.

Ms. **Martin**. We were concerned that we get the bill in in time to be considered this year, so we went ahead and introduced it.

Chairman **Gibbons**. You would not object, though, if we found no other serious objection to it, to including it in the initiative legislation?

Ms. **Martin**. Not if that would get it moved quickly.

Chairman **Gibbons**. Mr. Bailey?

Mr. **Bailey**. Thank you, Mr. Chairman.

Ron and Governor, I would like to invite you both here to argue and work on these issues—can you hear me?

Mr. **de Lugo**. If you are saying good things, please [laughter] there are some of my constituents back there.

Mr. **Bailey**. See, Governor, the trouble is he is a former drill sergeant, so you are so used to putting it out there, and if one of us poor young recruits comes back with it, it gets to be a little louder. So I'll try to speak up.

Ron, I want to compliment you particularly. I know how hard you have worked on these things, getting the messages across. And Governor, I would like to compliment you on a fine statement.

Has anybody sat down with you from the administration and really comprehensively gone over the impact of the net effect on investment, for example, or the extension of the investment tax credit, how it will accelerate the investment tax schedules, and how the advantage of that will purportedly help you?

Do you really think they are going to attract that much assistance or assist you that much on the island? It almost seems like somebody said that they are going to give something to you on one hand, at least in terms of the rum industry, and take away something on the other.

I may be wrong; I do not know if the administration has discussed this with you, but as I see it, there is not only a problem on the impact on your rum industry in terms of the excise tax issue, that is, supposedly revenues will be rebated to you, but as you mentioned very properly, you lose the industry. The net effect is to lose the industry.

I do not think there is much security for you in that arrangement, quite frankly. But I am just wondering if the net impact on other industries also has been considered. What is the nature of the aluminum industry? Have they gone over with you the effect on all of your industries?

For example, is it possible that tourism, which is so important to you, will be able to take advantage of some of these investment tax credit opportunities that will be available to American firms who want to invest in that aspect of Caribbean trade? Have those things been gone over with you at all?

Governor LUIS. Well, the tax measures have been discussed, but no one has come up with concrete figures as to adverse impacts. So we are dealing on concepts, and certainly, yes, we have dealt with specific problems, and for this reason we have recommended specific solutions to these.

But the overall adverse impact of the CBI on the Virgin Islands has not been determined at this point.

Mr. BAILEY. So there has not been an overall evaluation, maybe because there cannot be, maybe because we do not know. But even that has not been said to you, apparently. The net impact of the Caribbean Basin Initiative on investment in your area—is it conceivable the overall effect would be to discourage investment in your area?

Governor LUIS. I would say that if the recommendations that we have posed here are not carried out, then the CBI that is proposed, the Caribbean Basin Initiative, would definitely do us harm. I understand the same situation will happen with the island of Puerto Rico.

And our point is that we laud the effort to stem communism in the Caribbean and what have you, but we are saying that we are American territories, protect us first and then protect the other countries.

Mr. BAILEY. You know, I do not think that is a bad idea you just stated there. I do not think it is a bad idea at all.

I have a problem with the mix of diplomatic and military objectives sometimes with trade policy, because in my infant knowledge of the area—and I say that humbly and sincerely—the more I learn about it, the more it appears to me that some of those problems are highlighted, in effect, by distorting trade rules, causing a great deal of dissension, for example, here at home, and making it difficult to develop the kind of foreign policy that we need.

I just think in the long run that sometimes our goals are laudable, and I think the way you stated it is about the best way we can. The goals are laudable, the intentions are pure, but the mechanism is perhaps in the long run not the best way to do things.

Governor LUIS. The other problem I see is that this plan may be implemented and if not implemented properly would do harm to Puerto Rico and the Virgin Islands. What if we get the plan off base and then we do not contain communism.

Mr. BAILEY. Governor, you have served in the Army. I know what your feelings are and what your views are. I am glad you did not go on to play baseball, by the way. I think you are better where you are.

Governor LUIS. Thank you.

Mr. BAILEY. One of the things Ron mentioned that really interested me is the extension of some of those standards, wage standards, for example. I really wonder sometimes how much is accomplished by the kind of investment that we are going to attract to these areas, the real social and political impact of spending money in the Caribbean Basin without extending the kind of other things that, for example, have been extended to Puerto Rico and the Virgin Islands, that are very much a part of American expansion and growth—part of the culture, part of the respect for environmental concerns, part of the respect for due process rights, part of the respect for working conditions, and those kinds of things.

I really think that maybe in this initiative we ought to pay attention, if we are going to use the carrot, that the carrot be embellished with some things that make it particularly attractive to fostering the kinds of things that I know we both want.

I applaud you because I think what you are really saying to us is: Look, a growth, an increase in American concern in the Caribbean Basin is a good and proper thing. But maybe we are proceeding with rather a jaundiced and unexamined view of its overall impact, and it is going to be harmful to what we have established there already. I happen to agree with you.

Baltasar Corrada is up next, and he is a very good friend of mine and a hard-working man. I wonder what the net impact on Puerto Rico is. Myself, I have a tendency to think, when it all comes out in the wash it's going to be negative. I really do.

You say you have an aluminum industry there. I have never been to the Virgin Islands, incidentally.

Governor LUIS. We import bauxite and the bauxite is processed, and we do produce alumina, not aluminum. The alumina is then shipped elsewhere and that is used to be converted to aluminum.

Mr. BAILEY. How many people do you employ in that industry, do you know offhand? That may not be a fair question.

Governor LUIS. It is about 500 people.

Mr. BAILEY. 500 people in that industry. Has anybody commented on how that industry might be affected by the CBI? Right now you would have an advantage, probably. But how would it be affected under the CBI, do you know?

Governor LUIS. Relaxing the 30-percent withholding tax would help them, because this would encourage them to bring in a partner to help them expand their operations.

Mr. BAILEY. But that is not part of the CBI, or is it a part?

Governor LUIS. No, it is not. We are recommending reduction of the 30-percent withholding tax to help existing industries and to help us attract new industries, because if we are going to talk about investments to help the economies of these island nations in the Caribbean, we on our own are already sounding the warning that the 30-percent withholding tax is a great deterrent to accomplish this. We recognized this and we have taken the initiative before the CBI plan came on to help resolve this problem.

What we are saying is the CBI does not recognize this in the legislation presented to Congress.

Mr. BAILEY. The very least we can do is try to modify it to look out for the interest of our own territories.

Governor LUIS. We are urging this committee, based on the presentations that Mr. de Lugo and myself have presented, to amend the legislation where possible where our recommendations could improve the CBI, so that our position can be improved.

Mr. DE LUGO. May I speak to some concerns you have raised? They are the very concerns that we in the Virgin Islands and

Puerto Rico have. First of all—before I get into that, let me say that the accelerated cost recovery system and the investment tax credit would of course help Martin-Marietta, as it would Hess.

Mr. BAILEY. You do not have a Mazda plant down there, do you? Go ahead.

Mr. DE LUGO. We do need the 30-percent reduction to 10 percent, as the Governor pointed out. But these are things we have to give them to hope they will stay there in the U.S. territory, because one of our concerns—and Martin-Marietta has given no indication of this; I want to make that clear—but our concern is that, these industries that are located at the present time in U.S. territories, when we make it so attractive to go foreign, why will they not pull up and go foreign?

There are cheaper wages, you know, all of the environmental——

Mr. BAILEY. That is precisely my question.

Mr. DE LUGO. What has kept them in the U.S. territories up to the present time? The fear of political instability in the other areas. So the CBI takes care of that. It is now going to give to the American investor that goes foreign an assurance that if his property is expropriated he is reimbursed totally by the U.S. Government. So that is taken care of.

So if you are businessmen, where are you going to go? That is our concern in the U.S. territories. That is our fear, and that is why we have been negotiating with the administration and saying, look, we are Americans, we want to help you with this CBI policy, we applaud what you are trying to do, but for God's sake take the time out to put in some safeguards to protect the U.S. territories and the U.S. citizens in these territories or we are going to be down the tubes.

Mr. BAILEY. That is an excellent statement of my fears. Let me add to that a request—and then I will finish up, and I thank you for being patient with me—that some kind of work be done on what the potential impact on the tourist industry is going to be.

As far as exporting American political culture and democracy is concerned, which is our ultimate goal, I do not know if those interests are really served sometimes by a tourist industry that in many, many ways might be going away from our American territory, from Puerto Rico, from the Virgin Islands to areas that really provide, in my opinion, a good potential. It is a way of getting American dollars there, which is what this whole thing is all about. That is really all that it is, tying them to us and making them dependent upon us.

I do not know what the impact on tourism would be, and I would hope that you could get with the administration and get some feedback on that because that can represent a sizable investment too. You know, you build that airport and it ends up in the diversion of tourist dollar not meaning that much to you.

I wish you would look at that. It is not that we do not want to help these countries; it is just that we want to do it to the best interest of everyone concerned. I do not know if this is the ideal way to do it. I do not know how many goods are going to come through there, be processed elsewhere and have an add-on, and come in here, to your detriment, and I think to the detriment of some of those countries.

Governor LUIS. I agree an assessment should be made also in the tourist side. Once these countries begin to improve because they become more competitive, naturally they will then tend to improve their tourist trade, and an economic study should also be made in this area, and the impact of the CBI should also be studied further.

Mr. BAILEY. Thank you, Governor.

Thank you, Mr. Chairman.

Chairman GIBBONS. Surely.

Mr. Frenzel.

Mr. FRENZEL. Thank you, Mr. Chairman.

I am grateful to both gentlemen for their testimony.

I wanted to ask about the remission of excise taxes. Can you tell us what your revenues of the excise taxes from rum have been in the most recent year?

Governor LUIS. We have the revenues here explained since 1975, and they have been running as follows: fiscal year 1975, $17 million; 1976, $18.9 million; fiscal year 1977, $19.8 million; fiscal year 1978, $22.4 million; fiscal year 1979, $26 million; fiscal year 1980, $36 million; fiscal year 1981, $37.3 million; and fiscal year 1982 projected to be $40 million.

So you can see this is increasing with each fiscal year, each coming fiscal year.

Mr. FRENZEL. That is a pretty good deal. That is worth $200,000 per job in the rum industry down there. You have got 100 people making rum and you get $40 million back, which is in addition to whatever you get for selling the rum. That is a fairly high return now, isn't it?

You are coming in here and, as I understand your proposal, you are asking for a good deal more plus some guarantees. It seems like you are getting a fair amount out of this rum. I would like to make rum and get back that kind of money on it.

Mr. DE LUGO. If that money were not available to us, there would be additional dependency funds we would have to go after. That money is put into the operation of the Government of the Virgin Islands, and that was a decision of this committee and the Congress. I don't think we are asking for anything more. We are asking that we safeguard that industry and safeguard those funds because they account for some 18 percent of our total revenue in the running of our government.

It has been pointed out these territories sitting out in the middle of the Caribbean don't have the resources and that is why Congress has given us these tools, consciously created these tools so we could build our infrastructure.

Mr. FRENZEL. Ron, you suggested a 75/25-percent split. What is the market share between Puerto Rico and the Virgin Islands, about 90/10?

Mr. DE LUGO. It is about 90/10.

Mr. FRENZEL. In the 1979 MTN implementation bill, you were given some kind of a safeguard against the change from the wine gallon to the proof gallon. Can you tell me how much extra you got out of that?

Mr. DE LUGO. To my knowledge, that has not been implemented and we have not gotten anything out of that bill.

Mr. FRENZEL. OK, thank you very much.

You are also recommending in that bill we put those tax rebates on appropriations basis, and you want to make them a direct rebate now. Do I understand your testimony correctly in that regard?

Mr. de Lugo. They are at the present time——

Governor Luis. The rum excise taxes?

Mr. Frenzel. Yes.

Mr. de Lugo. We are asking they be rebated in the same manner as the present excise taxes are rebated, and that does not take an annual appropriation.

Mr. Frenzel. The extra protection granted in 1979 was to be provided by an appropriation, I believe; is that correct?

Governor Luis. Yes.

Mr. Frenzel. And you have never gotten an appropriation because your rum sales did not decline.

Governor Luis. That is correct.

Mr. Frenzel. OK. And any extra protection that you get in this Act you do not want covered by appropriations; you want them to be automatically rebated.

Mr. de Lugo. Yes.

Governor Luis. That is correct.

Mr. Frenzel. Well again, Mr. Chairman, I want to thank the gentlemen for excellent testimony and to thank Congressman de Lugo for his patience in working with us over the years in a very complicated matter.

Mr. de Lugo. I want to thank you, and if I may, I would like to thank Congressman Frenzel. He knows how many times I have come to him when a piece of legislation has been introduced and I thought it would be harmful to my constituents, and I want to commend him because I know when I am moving legislation of my own and it is moving along, it is not too much fun to have somebody show up at the last minute to say, wait a minute, could you reconsider this thing? But Bill Frenzel has done that for me and the people of the Virgin Islands on numerous occasions, and I want to publicly thank you for that, Bill.

Governor Luis. Mr. Chairman and members of this committee, I want to thank you for——

Chairman Gibbons. Let me ask you a couple of more questions. Is the Jones Act requiring you to ship in American bottoms much of a handicap problem?

Mr. de Lugo. At the present time the Jones Act does not apply to the Virgin Islands. It applies to Puerto Rico. We are exempt.

Chairman Gibbons. I did not realize that.

Mr. de Lugo. We are the only area that is, and that goes back quite a ways.

Chairman Gibbons. How about on the withholding tax? Suppose the committee decided to reduce it to zero? Would that be acceptable?

Governor Luis. Mr. Chairman, on that point the legislation requires that locally we would be getting the authority to reduce it further on a case-by-case basis.

Chairman Gibbons. In other words, you want us to reduce it to 10——

Governor Luis. Give us the authority to deal with reducing it further.

Mr. DE LUGO. Selectively.

Chairman GIBBONS. That makes sense.

Mr. DE LUGO. As we see how it goes.

Chairman GIBBONS. Thank you very much.

Mr. DE LUGO. Thank you, Mr. Chairman.

I would like to submit later a further discussion regarding the minimum assembly test written into the watch bill.

Chairman GIBBONS. All right, fine.

[The following information was subsequently received:]

CONGRESS OF THE UNITED STATES,
HOUSE OF REPRESENTATIVES,
Washington, D.C., March 31, 1982.

Hon. SAM GIBBONS,
Chairman, Subcommittee on Trade of the Ways and Means Committee,
Rayburn House Office Building, Washington, D.C.

DEAR MR. CHAIRMAN: This letter is in response to the concerns you raised last week with respect to some of the proposed Virgin Islands amendments to H.R. 5900, the Caribbean Basin Economic Recovery Act.

TARIFF-RATE QUOTA ON FOREIGN RUM

First, we would like to emphasize that the proposed tariff-rate quota on foreign-produced rum would not in any way limit the absolute quantities of foreign rum that can enter the United States. Instead, the proposed tariff-rate quota would only limit the amounts that can enter duty-free under the CBI. In this regard, we feel the use of a tariff-rate quota to be preferred to the alternatives of an absolute quota or an imposed tariff on all imports.

Our proposal would allow qualifying Basin countries to enter duty-free up to 110 percent of the historical high levels of rum entering the United States from such countries. The computation of the historical high level could be similar to that of sugar ceilings. Such countries could continue to import unlimited amounts of rum into the United States in excess of the 110 percent figure, but these amounts would be subject to the applicable tariff duty in effect for non-Basin countries.

Additionally, the Virgin Islands could support some mechanism whereby the tariff-rate quota on foreign rum would be increased by up to 10 percent a year provided that the Virgin Islands industry did not suffer injury as a result of increased imports from qualifying Basin countries. We believe that this could be accomplished by providing the President with authority to grant such increases if total exports of Virgin Islands rum to the United States in the preceding calendar year did not fall below 95 percent of total V.I. exports in 1981 (the pre-CBI base year).

The tariff-rate quota on rum could be administered under the Tariff Schedules without presenting an administrative burden. As you know, the Bureau of the Census and the Treasury Department provide quantitative import statistics which are then made available through the Department of Commerce International Trade Administration and periodic trade publications. Eventual imposition of tariffs should the quotas be reached would not be difficult administratively.

Because of the particular vulnerability of the Virgin Islands unaged, bulk rum industry to tariff elimination, a tariff-rate quota for rum such as that proposed provides the minimum level of protection required to allow the Virgin Islands rum industry to compete effectively against foreign imports, which are not affected by such factors as environmental regulations, minimum wage laws, and other regulatory controls placed upon the Virgin Islands. It should also be emphasized that, since many Basin countries currently receive preferential treatment from EEC and other countries which is denied to the Virgin Islands, the proposed tariff-rate quota would provide qualifying Basin countries with combined access to world markets on terms more favorable than those available to V.I. producers.

The alternative, when combined with the heavy regulatory burdens faced by Virgin Islands rum producers, is likely to be shut-down of the territory's industry. Because of its critical importance to the revenue structure of the Virgin Islands Government, we simply cannot afford to lose this industry. We are certain that the Administration does not intend this effect, but we need your help to ensure that it does not.

WATCH LEGISLATION

Last Tuesday, you also expressed some concern that legislation I have introduced to revitalize the watch industry (H.R. 5758) may not accomplish its intended objective and encourage instead the creation of "pass through" operations which do not provide substantial benefit to the local economy. I can assure you that I do not support "pass through" companies and that my only objective in introducing the legislation is to ensure that one of the few successful manufacturing industries in the United States flag territories will be able to survive the shift in market demand over the past few years.

At its peak, the Virgin Islands watch industry provided more than 1300 jobs and since 1967 made direct economic contributions (wages and taxes) of nearly $100 million. Because of a recent market shift away from mechanical 17 jewel watches to quartz analog timepieces, more than half the industry has shut down and employment has dropped to fewer than 300 persons. The industry can survive if production can be shifted to meet market demand for the new watches, but existing tariff incentives under General Headnote 3(a) of T.S.U.S. are insufficient to allow manufacture of quartz analog timepieces. Moreover, the Territory's watchcase and bracelet industry, which is largely dependent on the watch industry, also might not survive unless the tariff incentives are amended.

H.R. 5758 was developed jointly by the U.S. Departments of Commerce and Interior to place the watch industry on permanently solid footing. The main feature of the bill involves the elimination of the foreign material limitation for watches under General Headnote 3(a) and the substitution of a supplementary incentive system tied to the amount of assembly operations actually performed in the Territory. I understand that the reservations you raised last Tuesday concern the elimination of the 70 percent foreign materials limitation.

It is important to understand that General Headnote 3(a) involves a two-part test before an eligible article can enter the United States duty-free. First, the landed cost of such article (in the case of watches) may contain no more that 70 percent foreign materials. Second, the eligible article must be manufactured or transformed into a separate Virgin Islands product identifiable by tariff classification (in this case watches). I would like to stress that the foreign material content limitation is not a value-added requirement and does not, by itself, ensure that a minimum amount of assembly operations will be performed in the Virgin Islands. Rather, the mechanism that ensures meaningful economic activity in the Territory is the Customs Service's interpretation of the manufacturing test, and in the particular case of watches, the allocation rules administered by the Commerce and Interior Departments. (See attached Final Annual Rules for Calendar Year 1982).

The supplementary incentive in H.R. 5758 would encourage firms to maintain or set up watch assembly operations suitable for nonconventional, quartz analog watches, the assembly of which requires capital equipment expenditures of at least $50,000 per firm. The supplementary benefit would take the form of a certificate issued to territorial producers based on a portion of their actual wage payments to permanent residents. The certificates would entitle the holder, either the territorial firm, or some other entity to whom it has been sold or transferred, to secure refunds of duty on direct imports into the customs territory of the United States of watches and watch movements up to the face value of the certificate to insular wages serves to encourage additional assembly operations in the insular possessions. Moreover, this relationship would help offset the advantages which low-wage countries, such as Hong Kong, enjoy over insular producers.

In short, removal of the foreign content limitations will not encourage the creation of "pass through" operations. Instead, H.R. 5758 is a carefully designed measure, developed by the Federal Departments which currently regulate the insular watch industry, to get our most successful light manufacturing industry back on track and able to meet new challenges from foreign competition.

I hope that this letter answers the concerns you raised last week. I have specifically confined the letter to those concerns. Under separate cover I will be writing requesting inclusion in the CBI package of other important issues which the Governor of the Virgin Islands and I raised at the hearing.

My staff would be happy to work with the Subcommittee staff in drafting appropriate amendments or resolving any technical problems that might arise. Please feel free to call on us at any time.

Warm regards,

RON DE LUGO,
Virgin Islands Delegate to Congress.

Enclosure.

[From the Federal Register, Mar. 11, 1982]

DEPARTMENT OF COMMERCE, INTERNATIONAL TRADE ADMINISTRATION—DEPARTMENT OF THE INTERIOR, OFFICE OF THE SECRETARY

ALLOCATION OF WATCH QUOTAS FOR CALENDAR YEAR 1982 AMONG PRODUCERS LOCATED IN THE VIRGIN ISLANDS, GUAM, AND AMERICAN SAMOA

Agency: International Trade Administration, Commerce; Office of the Assistant Secretary for Territorial and International Affairs, Interior.

Action: Final annual rules.

Summary: Pursuant to Section 3 of the Department's Codified Watch quota regulations (15 CFR Part 303), annual rules for calendar year 1982 are being adopted. The Departments are making several changes from the 1981 provisions.

Date: These rules are effective on March 10, 1982.

For additional information contact: Mr. Frank W. Creel, who can be reached on 202-377-1660.

Supplementary information: In accordance with Executive Order 12391 dated February 17, 1981, the Departments of Commerce and the Interior have determined that these rules do not constitute a "major rule" as defined by Section 1(b) of the Order. They are not likely to result in:

(1) An annual effect on the economy of $100 million or more;

(2) A major increase in costs or prices in either the public or private sector; or

(3) Significant adverse impact on the domestic economy or on the ability of U.S. enterprises to compete with foreign enterprises.

The General Counsel of the Department of Commerce has certified that this action will not have a significant economic impact on a substantial number of small entities. Finally, the Departments have determined that publication of these rules will impose no change in the information collection burden on the public. That burden is limited solely to those entities receiving the associated federal benefits and the information collection is made on ITA from 334P under OMB approval number 0625-0040. Accordingly, publication of these rules is consistent with the Departments' responsibilities under the Paperwork Reduction Plan Act of 1980.

The Departments published these rules in proposed form on December 10, 1981 (46 FR 30488 (1981)) and invited comments from the public. The only comment received was from the American Watch Association (AWA), a watch industry association of importers, assemblers, manufacturers and their suppliers.

The Departments had proposed to modify the so-called two-tier allocation system, originally adopted in the 1979 rules, by applying the special incentives they contained only to the reallocation of quota. The Departments noted that reliance on largely preassembled components, which the two-tier system was designed to discourage, was not a current problem. We also pointed to the additional safeguards against such "passthrough" operations adopted by the U.S. Customs Service in 1980.

The AWA urged the Departments not to "jettison" the two-tier system so that it would be "available in future years." The AWA noted that the system "is doing no apparent harm, and, indeed, stands as an important symbol of the Departments' continuing determination to maintain the highest possible standards for local labor contributions."

The Departments' proposal relates to a provision of the annual rules, and the two-tier system could be readopted if a need were shown to exist in future years. We agree, however, with the AWA's points about the harmlessness and symbolic significance of the two-tier system in view of these points and the fact that no comments favoring the proposed change were received, we have decided to retain the two-tier system.

The AWA also commented on the Departments' proposal to raise their ceiling on creditable wages from $17,000 to $18,000. The AWA suggested that a ceiling of $23,000 would be "much more closely in line with the GNP deflator over the past decade."

Until the 1976 allocation, the Departments credited wages up to the FICA maximum. In that year, the Departments adopted an independent ceiling lower than the FICA maximum in order "to provide an additional incentive for the employment and training of territorial residents in skilled labor and supervisory positions." (40 FR 54274 (1975).) Adoption of a 1982 ceiling of $18,000 would represent an increase since 1976 of 36%. In the same period the FICA maximum has increased by almost 111%. Adoption of AWA's suggestion to increase the 1982 ceiling to $23,000 would result in an increase of 74% over the 1976 ceiling. The ceiling would then be equal to about 77% of the current FICA maximum.

While the additional incentive sought by the Departments since 1976 would clearly be greater with adoption of the proposed ceiling of $18,000, the above analysis shows that adoption of the AWA's suggestion would not mean the effective abandonment of the Departments' policy. The difference between the ceiling and the current FICA maximum would still be substantial enough to encourage producers to consider the availability of territorial residents for positions requiring special skills and supervisory ability. Accordingly, the final rule establishes a new ceiling of $23,000.

The AWA also recommended that the Departments conduct an "examination" of the need to revise their assembly criteria with respect to quartz analog watches and to establish a standard not "less stringent" than the existing standard.

This recommendation was not phrased as a suggestion for revising the 1982 rules but as a project to be undertaken. We agree that there is such a need. The Departments will welcome, during 1982, specific recommendations for a new standard for possible inclusion in the 1983 rules.

No other comments were received. The proposed rules, modified to reflect the foregoing discussion are adopted in final as shown below.

Section 1. (a) A portion of the 1982 Virgin Islands quota determined in accordance with subsection (c) below will be allocated on the basis of (1) the net dollar amount of economic contributions to the Virgin Islands consisting of the dollar amount of wages, up to a maximum of $23,000 per person, paid by each producer during calendar year 1981 to Virgin Islands residents and attributable to each producer's headnote 3(a) watch and watch movement assembly operations plus the dollar amount of income taxes paid by each producer during calendar year 1981 attributable to its headnote 3(a) watch and watch movement assembly operations (excluding penalty and interest payments and deducting income tax refunds and subsidies paid by the Virgin Islands government during calendar year 1981), and (2) the number of units of watches and watch movements assembled in the Virgin Islands and entered by each producer duty-free into the customs territory of the United States during calendar year 1981.

(b) In making allocations under this formula, a weight of 80 percent will be assigned to the economic contributions factor and a weight of 10 percent will be assigned to the shipments factor. In calculating each producer's economic contributions, the Departments shall deduct from creditable wages any negative tax balances. That is, if the total of a producer's income tax payments during 1981 (excluding penalties and interest charges) is smaller than the total of refunds and subsidies received from the Virgin Islands government during 1981, the difference of the two sums shall be deducted from the producer's creditable wages for allocation purposes.

(c) An amount representing that portion of the 1982 Virgin Islands quota equal to the ratio of general headnote 3(a) shipments of watches and watch movements from the territory during 1981 to the total 1981 Virgin Islands quota will be allocated among the producers in the Virgin Islands, in accordance with the allocation factors and weights specified in (b) above.

Section 2. Sixty percent of the 1982 Guam quota may be allocated, pursuant to § 303.5(a)(4) of Title 15 of the Code of Federal Regulations, to the single Guam producer (see also subsection 3(B) and Section 6, below).

Section 3. (A) The portion of the Virgin Islands quota not allocated pursuant to Section 1, except as specified in Section 4, will be allocated among firms meeting the requirements of paragraph (1) or (2) of this section. Eligible firms will be allocated quota in accordance with the factors and weights specified in Section 1. Allocation of the portion of the Virgin Islands quota under this Section will be made to firms which: (1) Assembled all watch movements shipped during 1981 from unassembled movements having at least 26 discrete components and all watches (that is, cased movements) during 1981 from at least 29 discrete components, including at least 26 movement components and at least 3 case components: or (2) Made wage payments during 1981 in the territory averaging not less than $.75 per watch movement and $.95 per watch assembled and shipped into the customs territory of the United States. In determining a firm's eligibility under this criterion, the Departments may make appropriate data adjustments to take into account wages paid for the assembly of units not shipped during 1981 and shipments assembled prior to 1981.

(b) Allocation of the portion of the Guam quota not allocated pursuant to Section 2 may be allocated pursuant to § 303.5(b) of Title 15 of the Code of Federal Regulations.

Section 4. Quota set aside for new firms in the Virgin Islands under subsection 5(b) shall be subtracted from the quota amount allocable under Section 3, before allocation are made pursuant to that subsection.

Section 5. (a) Applications from new firms are invited for the calendar year 1982 American Samoa quota. Due to the limited size of the American Samoa quota, the

Departments will allocate that quota to the single firm which offers the best prospect of a meaningful long-term contribution to the economy of the territory.

(b) Applications from new firms are invited for 2,000,000 units of the calendar year 1982 Virgin Islands quota.

(c) Applicants for new-entrant quotas must complete applicable sections of Form ITA-334P, copies of which may be obtained from the Statutory Import Programs Staff, U.S. Department of Commerce, Washington, D.C. 20230. Detailed instructions for completing ITA-334P will be provided by the Statutory Import Programs Staff together with copies of the application form.

(d) The Departments will consider new entrant applications only from firms which certify to the Departments that they are able and willing to meet the minimum assembly or wage contribution criteria established in Section 3. Following the Secretaries' determination that a qualifying application has been received, an announcement will be published in the Federal Register establishing a closing date for further applications. The closing date shall be 30 days from the date of such notice. If the Departments do not receive prior to September 1, 1982, a qualifying application for quota set aside by subsection (b) above, that quota may be reallocated among eligible producers pursuant to § 303.5(b) of Title 15 of the Code of Federal Regulations.

Section 6. Reallocation of calendar year 1982 quota that becomes available will be restricted to those firms satisfying the criteria established in subsection 3(a), to any new entrant firms selected pursuant to Section 5 above, and to the new Guam firm, provided its operations at the time of the reallocation satisfy the criteria established in subsection 3(a).

Section 7. As used in Section 3 of these rules:

(a) "Wages" means all wages up to $23,000 per person paid to residents of the territories employed in a firm's headnote 3(a) watch and watch movement assembly operations. Excluded, however, are wages paid (i) accountants, lawyers, or other professional personnel who may render special services to the firm, (ii) persons assembling non-headnote 3(a) watches and watch movements, (iii) persons engaged in the repair of non-headnote 3(a) watches and watch movements, and (iv) persons engaged in the strapping and packaging of watches. Wages paid to persons engaged in both headnote 3(a) and non-headnote 3(a) assembly and repair activities shall be credited proportionately for their headnote 3(a) activities, provided the firm maintains production and payroll records adequate for the Departments' verification of the headnote 3(a) portion.

(b) "Discrete movement components" means screws, parts, components and subassemblies not assembled together with another part, component or subassembly at the time of importation into the territory. (A mainplate containing set jewels or shock devices, together with other parts, would be considered a single discrete component, as would a barrel bridge subassembly.) Excluded are dials, dial washer, dial screws, hour wheels, hands, automatic mechanisms and related parts, day-date mechanisms and calendar features, and jewels.

Section 8. (a) All firms must, as a condition for receipt of allocations or reallocations based on subsection 3(a) criteria, certify to the Departments that they will not alter assembly operations during calendar year 1982 in a manner which would result in their failure to satisfy the respective criteria.

(b) If the Departments have reason to believe that a producer has not complied with or is not complying with the certification required by subsection (a) of this section, they may issue an order requiring the producer to show cause within 30 days of receipt of the order why the duty free quota to which it would otherwise be entitled should not be cancelled or reduced by the Departments.

Section 9. (a) The quarterly reporting requirements of § 303.8(a) of the Code of Federal Regulations are suspended for calendar year 1982, and copies of Form ITA-321P will not be forwarded to producers at the times specified by that provision.

(b) Each producer must comply with § 303.8(b) of the Code of Federal Regulations and report any changes in ownership, interest and control which have occurred during any quarter by April 15, July 15 and October 15, respectively, but may do so by letter. (Pub. L. 89-805, 80 Stat. 1521 (19 U.S.C. 1202) as amended 15 CFR Part 303).

Issued at Washington, D.C. on March 4, 1982.

John L. Evans, Acting, Deputy Assistant Secretary for Import Administration, Department of Commerce.

Pedro A. Sanjuan, Assistant Secretary for Territorial and International Affairs, Department of the Interior.

Mr. DE LUGO. We will further explore the potential impact on the tourist industry.

Chairman GIBBONS. Because I do not really understand what you want on the watches, and I would like to just sit down and chat with you about that.

Thank you very much.

Next we have the congressman from Puerto Rico, Mr. Corrada.

Mr. Corrada, we welcome you here. We know the fine job you are doing, and I have discussed some of these matters with you. You may proceed as you wish.

STATEMENT OF HON. BALTASAR CORRADA, RESIDENT COMMISSIONER OF PUERTO RICO

Mr. CORRADA. Thank you, Mr. Chairman and members of the subcommittee.

I would like to ask that my full testimony, consisting of 15 pages and an attachment A, be made part of the record.

Chairman GIBBONS. Yes, sir, it will.

Mr. CORRADA. Mr. Chairman and members of the subcommittee, I appear today before this subcommittee as the only official directly elected by the people of Puerto Rico to represent them in the Congress of the United States to testify on the Caribbean Basin Economic Recovery Act.

As soon as I learned several months ago that the Reagan administration was considering a new CBI and that such initiative might involve policies to promote investment, trade and aid to foreign countries in Central America and the Caribbean, I became interested and concerned about the potential positive and negative impacts that the CBI could have on the economic and social development of Puerto Rico, the largest U.S. domestic area in the Caribbean.

A process of close consultation was developed between the executive branch of the Federal Government and the Governor or Puerto Rico and other Puerto Rican officials. In December we held hearings in the House Interior Committee to hear Reagan administration representatives describe policy options under consideration by a task force dealing with the development of policies for the CBI.

At that time, both Delegate Ron de Lugo of the U.S. Virgin Islands and I on behalf of Puerto Rico expressed the need to develop the CBI in a manner consistent with the best interests of our people.

It is my responsibility today, based on the overall package submitted to Congress as part of the bill under your consideration as well as other concessions made to us not embodied in this bill but covered by other actions and assurances given to us by the Reagan administration, to take a position on the CBI.

I would like to state at the outset that I have been and still am very critical of many of the policies of the Reagan administration as they affect or impact Puerto Rico, particularly the budget cutbacks and some of the concepts of the new federalism. However, in all fairness, having a sense of responsibility rising above partisan and parochial considerations, I must tell you today that as Resident Commissioner of Puerto Rico in this House, I strongly support President Reagan's Caribbean Basin Initiative as a bold and creative act of statesmanship which aims directly at the major problem of that important and neighboring area of the world, inadequate economic growth, which endangers regional stability and peace.

The nations in the Caribbean region run the spectrum of economic and social development. It is a region where contrasts are stark, all the landowning families living side by side with people barely able to keep themselves and their children fed. Conditions such as these make those countries particularly vulnerable to a revolution from either the right or the left.

A number of these countries are running huge deficits in the face of negligible or negative economic growth, increasing population, inflation in the worldwide economic recession. The escalation of violence and fighting in the region, particularly in Central America, bring increasing urgency to provide the economic framework within which these countries can recover and prosper.

I believe that the tools utilized in President Reagan's CBI proposal—investment, trade and aid—are precisely the ones required to promote the economic development and stability of the countries of the Caribbean Basin, and I am generally supportive of the bill.

I would like to address now some of the elements of this policy as they pertain to Puerto Rico. In his letter to Congress dated March 17 transmitting to us the CBI bill, President Reagan states that Puerto Rico and the U.S. Virgin Islands have a longstanding special relationship with the United States and that their development must be enhanced by our policy toward the rest of the region.

In that context the President reaffirmed his administration's commitment to the following treatment for Puerto Rico, and these are included in the bill pending before you. First, the accelerated cost recovery system and the investment tax credit will be extended to property used by companies operating in Puerto Rico and the Virgin Islands.

Second, excise taxes on all imported rum will be transferred to Puerto Rico and the Virgin Islands, and other measures may be taken by the President if rum revenues to Puerto Rico and the Virgin Islands are reduced, including the withdrawal of duty-free treatment of rum provided by this bill.

Third, inputs into Caribbean Basin production from Puerto Rico and the Virgin Islands will be considered domestic inputs from Caribbean Basin countries for purposes of the rules of origin. This will help Puerto Rico to develop the concept of twin plants and joint resource development with Caribbean Basin countries.

Fourth, industries in Puerto Rico and the Virgin Islands will have access to the same safeguard provisions as mainland industries under the Trade Act of 1974. This would allow industries, including agricultural and manufacturing industries, to petition the International Trade Commission for relief from serious injury or threats thereof resulting from increasing foreign competition in the U.S. market. Such relief may include an increase in U.S. duties on foreign products or tariff rate quotas or quantitative restrictions on imports or the negotiation of orderly marketing agreements or any combination thereof.

Fifth, the tropical agricultural research facility at Mayaguez, Puerto Rico will be used to further the agricultural development of the Caribbean Basin.

These specific safeguards are contained in the Caribbean Basin Economic Recovery Act bill sent by President Reagan to Congress. I am pleased by these features in the bill and I urge you to make sure that any bill reported by the subcommittee retains and strengthens these provisions.

There are other assurances and concessions made to us by the Reagan administration arising from the discussion with them of the CBI which will be addressed in separate bills or by other actions in addition to those specifically covered by the bill under your consideration.

In a fact sheet given to us by Reagan administration officials, certain commitments were made to us. They are spelled out in my testimony. I am not going to, for the sake of time, read them to you, but they involve important new policies in the field of agriculture and transportation.

They include the support for a bill that I have introduced, H.R. 1489, which would allow the transportation of passengers between Puerto Rico and the mainland United States in foreign-flag vessels as long as there is no American-flag vessel willing and able to provide the service.

That is the current situation. There are other provisions that pertain to aid, procurement, environmental regulations, crude refinery facilities, oil explorations, and the involvement of Puerto Rican officials in the bilateral discussions pertaining to the CBI.

I will continue now on page 10 of my testimony. While Puerto Rico will benefit by the proposed legislation and these other actions, we must overcome major and growing economic problems. Some of these are structural: sharp increases in electrical, process energy and transportation costs, unemployment of more than 22 percent, substantial unemployment, and a labor force participation rate of about 41 percent versus more than 60 percent for the mainland.

The latter reflects the large pool of people willing but not able to find work, and insufficient technical and language training. These structural problems, in combination with the deep U.S. recesssion, ever growing low wage country competition for Puerto Rican products on the U.S. market, and existing and projected real reductions in Federal aid make our development task massive.

We have been successful and will continue to promote our industries such as electronics, scientific and pharmaceutical industries, but we are substantially dependent on the more labor-intensive industries such as food, tobacco, textiles, apparel, and leather products.

In 1967 these industries provided 70,508 jobs or 76 percent of the total manufacturing employment of 135,287. Employment in these industries dropped to 68,500 in May 1981 but still represented 44 percent of total manufacturing employment of 154,600 workers. Apparel alone employed 37,755 in 1967 or 28.5 percent of manufacturing employment, and in May 1981, it still provided 33,500 jobs, or 22 percent of manufacturing employment.

Our refining and petrochemical industry has been seriously injured by the foreign oil price explosion. Even with average domestic oil prices now approaching foreign prices, mainland processing costs are substantially lower than Puerto Rican costs. Our largest refinery has closed and several important petrochemical plants as well.

Clearly, the elimination of duties or, in the case of textiles and apparel, transfer of sales quotas from Far Eastern countries to the Caribbean Basin may adversely affect Puerto Rican production and sales to the U.S. market. For example, from fiscal year 1967 to 1976, a period congruent with the Kennedy Round and a large increase in labor-intensive imports from low-wage countries, 23,400 manufacturing jobs were lost in 913 closed plants whose establishment was promoted by the Puerto Rico Economic Development Administration.

In total, all plant closures during this period cost 31,300 jobs, plus thousands of other jobs lost as an indirect effect. From fiscal year 1972 through the first 9 months of fiscal year 1975, 300 plants closed, including 21 textile, 99 apparel, 25 electrical equipment and machinery, 19 furniture, 19 leather, 15 plastic and 12 chemical product plants.

I am struck by the fact that in recent conversations with the executive branch concerning the impact of CBI, on trade and tax measures we were informed that studies had not been made of the effects of duty-free imports and individual U.S. industries. I believe the administration should determine what new industries are likely to be established and the effect of greater imports on existing and new Caribbean Basin products on individual U.S., including Puerto Rican, industries.

In summary, the current U.S. recession, worldwide trends involving shifts of labor-intensive production from developed to developing countries, combined with increasing developed country specialization in high technology industries, our structural problems and reduced Federal assistance force us not only to accelerate development to provide employment for our youth, other unemployed and discouraged applicants outside the work force, but to strengthen and to rapidly convert threatened industries into nationally and internationally competitive industries.

This requires not only continuing but strengthening and expanding Federal tax incentives for Puerto Rico, combined with our own major self-help measures to strengthen technical education and language training, assist small business to expand and create jobs, expand our tax base and increase our own revenues to replace lost Federal resources.

For these reasons I believe it is essential and I recommend that the administration and Congress address other important measures both in the context of the CBI as well as in terms of the general responsibility of the Federal Government to provide for the well-being of the U.S. territories and possessions and the American citizens of Puerto Rico.

Among these measures I recommend first phasing in of equal treatment for Puerto Rico in Federal programs from which we are excluded or where our share is below what we would receive if treated like a State. In attachment A I point out which are those policy areas.

Second, request the United States Special Trade Representative, the Department of Commerce and the ITC to present to this subcommittee a commodity-by-commodity analysis of the effects of one-way free trade on agriculture and manufacturing industries in the United States, including Puerto Rico.

For those commodities identified by the study as endangered by duty eliminations, this subcommittee should consider either not eliminating or phasing in duty elimination over a reasonable period. Equally important, safeguard measures should be strengthened by making it easier for U.S. industries, including those in Puerto Rico, to prove injury or the threat of injury from duty-free Caribbean Basin imports and easier to establish the need for relief in the event of market disruption for regional markets such as Puerto Rico.

Third, continuation and strengthening of an adjustment assistance program related to the CBI initiative and establishment of an early warning system to identify threatened industries and plants before they are damaged and to help them become more competitive, produce new products, save and expand jobs.

Fourth, strengthening the Federal tax incentive program and supporting section 936 and related provisions in the Internal Revenue Code to help us help ourselves in overcoming our difficult structural and employment problems and overcome the severe erosion of our competitive position stemming from the OPEC-induced massive increase in energy, raw material and transportation costs and from the recent sharp reduction in Federal corporate taxes.

Fifth, the extension to Puerto Rico, as proposed in the CBI bill, of the 1981 accelerated cost recovery system and investment tax credits and the extension of R. & D. benefits as major new development tools.

Sixth, a strong Federal policy for the development of maritime transportation including ports development, airport and ground transportation infrastructure in Puerto Rico is necessary to be consistent with the administration's plans under CBI to develop Puerto Rico into a major transportation hub for the Caribbean.

I respectfully submit that it is vital to address and resolve these issues to enable Puerto Rico help itself to achieve economic development and social justice and to enable us to become a major participant and positive force in achieving the administration's objectives of rapid economic growth, stability and peace in the Caribbean Basin.

[The prepared statement follows:]

STATEMENT OF BALTASAR CORRADA, RESIDENT COMMISSIONER OF PUERTO RICO

I appear today before this Subcommittee as the only official directly elected by the people of Puerto Rico to represent them in the Congress of the United States to testify on the Caribbean Basin Economic Recovery Act.

As soon as I learned several months ago that the Reagan Administration was considering a new Caribbean Basin Initiative ("CBI") and that such initiative might involve policies to promote investment, trade and aid to foreign counties in Central America and the Caribbean, I became interested and concerned about the potential positive and negative impacts that the CBI could have on the economic and social development of Puerto Rico—the largest United States domestic area in the Caribbean. I wrote letters to Assistant Secretary of State for Latin American Affairs Tom Enders and to International Trade Negotiator Ambassador Bill Brock, in October and November of last year warning them that the CBI policies had to be developed with great care to insure that not only Puerto Rico and the U.S. Virgin Islands would not be injured by such policies but that in fact these U.S. domestic areas in the Caribbean would benefit and prosper under any forthcoming proposal. The Governor of Puerto Rico, Hon. Carlos Romero Barcelo and others in Puerto Rico as well expressed their concern to the Reagan Administration on the matter. A process of close consultation was developed between the executive branch of the federal government and the Governor of Puerto Rico and other Puerto Rican officials. In December we held hearings in the House Interior committee to hear Reagan Administration representatives describe the policy options under consideration by a task force dealing with the development of policies for the CBI. At that time both Delegate Ron de Lugo of the U.S. Virgin Islands and I, on behalf of Puerto Rico, expressed the need to develop the CBI in a manner consistent with the best interest of our people.

Governor Romero presented the Reagan Administration with an extensive document on December 17, which I fully supported, outlining our general concerns as well as specific proposals requesting concessions, safeguards and other measures we deemed important to adequately protect, preserve and further develop the Puerto Rican economy within the context of the CBI as well as in terms of the general responsibility of the federal government to provide for the well-being of the U.S. territories and possessions and Puerto Ricans as citizens of the United States. As in any process of negotiation and discussion we were successful in obtaining from the Reagan Administration a commitment to support some of the concessions, safeguards and measures we wanted but not all of those outlined in our proposals, some of which are still the subject of discussions outside the context of the CBI. However, it is my responsibility today, based on the overall package submitted to Congress as part of the bill under your consideration as well as other concessions made to us not embodied in this bill but covered by other actions and assurances given to us by the Reagan Administration to take a position on the CBI.

I would like to state at the outset that I have been and still am very critical of many of the policies of the Reagan Administration as they affect or impact Puerto Rico, particularly the deep and severe budget cutbacks in many federal domestic programs such as the CETA jobs program, food stamps, housing, education, health, EDA, Farmers Home Administration and many others. I have been and am highly critical of President Reagan's policies about the so-called "New Federalism" which in my mind would represent a retrenchment on the part of the federal government from its responsibilities to promote the well-being of the poor, the ill-educated, the sick, the elderly, the children, the minorities and the working middle class of America, including the people of Puerto Rico. However, in all fairness and with a sense of responsibility rising above partisan and parochial considerations, I must tell you today that as Resident Commissioner of Puerto Rico in this House, I strongly support President Reagan's Caribbean Basin Initiative as a bold and creative act of statesmanship which aims directly at the major problem of that important and neighboring area of the world-inadequate economic growth which endangers regional stability and peace.

The nations in the Caribbean region run the spectrum of economic and social development. From a literacy rate of between 10–12 percent and a per capita income of $260 a year for the over five million citizens of Haiti, to a literacy rate of 95 percent and a per capita income of $3,960 for the 1.17 million citizens of Trinidad-Tobago. Per capita income is even higher—$4,650—for the Bahamians.

It is a region where contrasts are stark, wealthy, landowning families living side by side with people barely able to keep themselves and their children fed. Conditions such as these make those countries particularly vulnerable to revolution from either the right and the left. A number of these countries are running huge deficits in the face of negligible or negative economic growth, increasing population, inflation and the world-wide economic recession. An illustration is Jamaica with a negative real economic growth rate in 1979 of 2.3%, on the one hand, and Honduras with a 6.7% real economic growth in 1979 on the other. Even Costa Rica, the long time model of democracy and economic development of the region, is not safe from economic turmoil.

In addition, the escalation of violence and fighting in the region bring increasing urgency to provide the economic framework within which these countries can recover and prosper. I believe that the tools utilized in President Reagan's CBI proposal—investment, trade and aid—are precisely the ones required to promote the economic development and stability of the countries of the Caribbean Basin and I am generally supportive of the bill.

The need to promote the development and stability of the countries of the Caribbean Basin should be recognized by the United States and by Puerto Rico as a U.S. domestic area in the Caribbean.

I would like to address now some of the elements of this policy as they pertain to Puerto Rico.

In his letter to Congress dated March 17 transmitting to us the CBI bill, President Reagan states that "Puerto Rico and the U.S. Virgin Islands have a long-standing special relationship with the United States" and that "their development must be enhanced by our policy toward the rest of the region." In that context, the President reaffirmed his Administration's commitment to the following treatment for Puerto Rico.

First, the accelerated cost recovery system (ACRS) and the investment tax credit (ITC) will be extended to property used by companies operating in Puerto Rico and the U.S. Virgin Islands.

Second, excise taxes on all imported rum will be transferred to Puerto Rico and the Virgin Islands and other measures may be taken by the President if rum revenues to Puerto Rico and the Virgin Islands are reduced, including the withdrawal of duty free treatment of rum provided by this bill.

Third, inputs into Caribbean Basin production from Puerto Rico and the Virgin Islands will be considered domestic inputs from Caribbean Basin countries for purposes of the rules of origin. This will help Puerto Rico to develop the concept of "twin plants" and joint resource development with Caribbean Basin countries.

Fourth, industries in Puerto Rico and the Virgin Islands will have access to the same safeguard provisions as mainland industries under the Trade Act of 1974. This would allow industries, including agricultural and manufacturing industries, to petition the International Trade Commission for relief from serious injury or the threat thereof resulting from increasing foreign competition in the U.S. market. Such relief may include an increase in U.S. duties on foreign products or tariff-rate quotas or quantitative restrictions on imports or the negotiation of orderly marketing agreements or any combination thereof.

Fifth, the tropical agricultural research facility at Mayaguez, Puerto Rico will be used to further the agricultural development of the Caribbean Basin.

These specific concessions or safeguards are contained in the "Caribbean Basin Economic Recovery Act" bill sent by President Reagan to Congress. I am pleased by these features in the bill and urge you to make sure that any bill reported by the Subcommittee retains and strengthens these provisions.

There are other assurances and concessions made to us by the Reagan Administration arising from the discussion with them of the CBI which will be addressed in separate bills or by other actions in addition to those specifically covered by the bill under your consideration.

In a fact sheet given to us by Reagan Administration officials the following commitments were made to us:

I. AGRICULTURE

(a) Crop Insurance—The Department of Agriculture will extend to Puerto Rico through the Federal Crop Insurance Corporation its reinsurance program no later than mid-1983 provided certain technical problems can be overcome.

(b) Price Supports—The Department of Agriculture will extend to Puerto Rico price supports for rice and will consider the possibility of extending to Puerto Rico price supports for all commodities produced in Puerto Rico for which there is a U.S. price support program.

(c) Puerto Rican Agricultural Development—The Federal government, through the Department of Agriculture or other agencies, will provide techical asistance to Puerto Rico upon request for the purpose of improving the productivity of the island's agriculture.

Technical Assistance will also be given to Puerto Rico upon request in an effort to integrate the island's agricultural development with that of the Caribbean Basin as a whole.

The Federal government will also make greater use of the Tropical Agriculture Research Center, located in Puerto Rico, for the purpose of developing and implementing an integrated Caribbean Basin agricultural strategy.

II. TRANSPORTATION

(a) Air negotiations—The U.S. Government should seek to expand air routes between and through San Juan and foreign countries for American and foreign flag carriers.

In future bilateral air negotiations account will be taken of the vital importance of increasing foreign carrier entry into Puerto Rico. Prior consultation between Puerto Rican officials and U.S. negotiators should be undertaken regularly.

U.S. flag carriers should be able to take advantage of San Juan's status as the transportation hub of the Caribbean. For Caribbean nations, the U.S. should seek a liberal entry regime for U.S. carriers between Puerto Rico and Caribbean nations.

These policies should be negotiated with a view to achieving Puerto Rico's objectives, including the establishment of a Canada-Puerto Rico air route and new or additional air routes between Puerto Rico and Mexico, Venezuela, Brazil and the United Kingdom.

(b) Cruise Ships—The Administration will submit to the U.S. Congress an amendment to existing legislation to permit cruise ship passengers on foreign flag carriers to travel: (1) between San Juan and other U.S. ports; and (2) between U.S. ports and San Juan without restrictions as long as there exist no U.S. flag carriers available to provide adequate service between U.S. ports and San Juan or vice versa.

I have already introduced legislation to this effect, H.R. 1489, and the Subcommittee on Merchant Marine will hold hearings shortly on this bill in San Juan.

The current restriction limiting the number of hours a cruise ship or cruise ship passengers can remain in the port of San Juan shall be extended from 24 hours to an unlimited stay in port.

(c) Shipping to Puerto Rico—The Department of Transportation is studying carefully its regulations affecting cost of shipping for Puerto Rico, with a view to modifying those regulations where Puerto Rican economic development is being retarded. Consideration should be given to specific requests from Puerto Rico in the area of rate setting and financing vessels.

III. AID

Aid Procurement—Aid will make a strong effort to secure material inputs, technical assistance contracting and institutional support from Puerto Rico.

IV. ENVIRONMENTAL REGULATIONS

EPA will review, at Puerto Rico's request, the application of its regulations to the Islands. EPA will endeavor to be more flexible in future application of regulations having a substantal impact on these areas.

V. CRUDE REFINERY FACILITY

If justified by feasibility studies, the Departments of State and Energy will promote Puerto Rico as a center for refinery of heavy crude. The State Department and Department of Energy will bring to the attention of the region the possibility of using Puerto Rican facilities for heavy crude refining and the export of lighter crudes or products.

VI. COPPER AND OIL EXPLORATIONS

The Federal government will continue to provide to Puerto Rico where appropriate, technical assistance for the purpose of assisting the exploration and development of cooper, oil or other natural resources.

VII. CBI IMPLEMENTATION

Puerto Rican officials are deeply interested in participating in the design and implementation of the CBI. The U.S. Government has in fact, consulted very closely with these officials on all aspects of the CBI and intends to continue to do so. Puerto Rican officials will be invited to participate in many of the bilateral discussions involving CBI implementation.

While Puerto Rico will benefit by the proposed legislation and by other actions we must overcome major and growing economic problems. Some of these are structural: sharp increases in electrical, process energy and transportation costs, unemployment of more than 22 percent, substantial underemployment and a labor force participation rate of abot 41 percent versus more than 60 percent for the mainland.

The latter reflects a large pool of people willing but not able to find work and insufficient technical and language training.

These structural problems in combination with the deep U.S. recession, ever growing low-wage country competition for Puerto Rican products in the U.S. market and existing and projected real reductions in federal aid make our development task massive.

Federal grants to the Puerto Rican Government increased from $492 million in fiscal year 1973 to $833 million in fiscal year 1976 and to $1,309 million in fiscal year 1980. In fiscal year 1980 total federal disbursement in Puerto Rico were $4,269 million ($4.26 billion) including transfer payments, federal operating expenses and returned excise taxes and customs duties. After deducting $734 million in payments to the Federal government, net federal disbursements were $3,535 million or 31.8 percent of Puerto Rican gross product. Without considering the reductions proposed under the New Federalism, the real reductions in assistance to Puerto Rico in fiscal year 1982 compared with fiscal year 1981 are in the several hundred million dollar range including the shift from Food Stamp to the Nutritional Assistance Block Grant, near elimination of Federal Economic Development Administration programs, a loss of 25,000 CETA jobs and $140 million of employment and training programs and other reductions.

We were very successful in Puerto Rico in increasing our gross domestic product and our per capita personal income respectively from $754.5 million and $296 in 1950 to $11,104.8 million and $3,494 in 1980, but growth declined sharply in fiscal year 1980, was essentially stagnant in fiscal year 1981 and like the U.S. economy, is declining now.

We have been successful and will continue to promote the growth of our internationally competitive high technology, high wage industries such as electronics, scientific instruments, pharmaceuticals and others, but we are still substantially dependent on the more labor intensive industries such as food, tobacco, textiles, apparel, and leather products. In 1967 these industries provided 70,508 jobs or 76 percent of total manufacturing employment of 125,287. Employment in these industries dropped to 68,500 in May, 1981 but still represented 44 percent of total manufacturing employment of 154,600. Apparel alone employed 37,755 in 1967 or 28.5 percent of manufacturing employment, and in May 1981 still provided 33,500 jobs or 22 percent of manufacturing employment.

Our refining and petrochemical industry has been seriously injured by the foreign oil price explosion. When foreign oil was cheaper than domestic oil, Puerto Rico was excepted from the mandatory oil import quotas as a U.S. government policy and as a major incentive to overcome higher shipping transport costs from Puerto Rico to the U.S. market and to create a refinery and petrochemical industry. This was to be the basis for downstream fabrication plants and thousands of jobs. Even with average domestic oil prices now approaching foreign prices, mainland processing costs using domestic gas and oil are substantially lower than Puerto Rican costs. Our largest refinery has closed as have several important petrochemical plants.

Clearly, elimination of duties (or in the case of textiles and apparel, transfer of sales quotas from Far Eastern countries to the Caribbean Basin) may adversely affect Puerto Rican production and sales to the U.S. market.

For example, from fiscal years 1967 to 1976 (a period congruent with the Kennedy Round and a large increase in labor intensive imports from low wage countries) 23,400 manufacturing jobs were lost in 913 closed plants whose establishment was promoted by the Puerto Rico Economic Development Administration. In total all plant closures during this period cost 31,300 jobs plus thousands of other jobs lost as an indirect effect.

From fiscal year 1972 through the first nine months of fiscal year 1975, 300 plants closed including 21 textile, 99 apparel, 25 electrical equipment and machinery, 19 furniture, 19 leather, 15 plastic and 12 chemical product plants.

I am struck by the fact that in recent conversations with the Executive Branch concerning the impact of Caribbean Basin trade and tax measures we were informed that studies had not been made of the effects of duty free imports on individual U.S. industries. I believe that the Administration should determine what new industries are likely to be established and the effect of greater imports on existing and new Caribbean Basin products on individual U.S. including Puerto Rican industries.

In summary, the current U.S. recession, world wide trends involving shifts of labor intensive production from developed to developing countries combined with increasing developed country specialization in high technology industries, our structural problems and reduced federal assistance, force us not only to accelerate development to provide employment for our youth, other unemployed and discouraged applicants outside the workforce but to strengthen or rapidly convert threatened industries into nationally and internationally competitive industries.

This requires not only continuing but strengthening and expanding federal tax incentives for Puerto Rico combined with our own major self help measures to strengthen technical education, and language training, assist small business to expand and create jobs, expand our tax base and increase our own revenues to replace lost Federal resources.

For these reasons I believe it essential and I recommend that the Administration and the Congress address other important measures both in the context of the CBI as well as other federal policies on Puerto Rico:

1. Phasing in of equal treatment for Puerto Rico in federal programs from which we are excluded or where our share is below what we would receive if treated like a state. See attachment A.

2. Request the U.S. Special Trade Representative, the Department of Commerce and the International Trade Commission to present to this Subcommittee a commodity by commodity analysis of the effects of one-way-free trade on agriculture and manufacturing industries in the United States including Puerto Rico.

For those commodities identified by the study as endangered by duty eliminations, this Subcommittee should consider either not eliminating or phasing-in duty elimination over a reasonable period. Equally important, safeguard measures should be strengthened by making it easier for U.S. industries to prove injury or the threat of injury (from duty free Caribbean Basin imports) and easier to establish the need for relief in the event of market disruption for regional markets such as Puerto Rico.

3. Continuation and strengthening of an Adjustment Assistance Program related to the CBI Initiative and establishment of an early warning system, to identify threatened industries and plants before they are damaged and to help them become more competitive, produce new products, save and expand jobs.

4. Strengthening the Federal tax incentive program and supporting Sec. 936 and related provisions in the Internal Revenue Code to help us help ourselves in overcoming our difficult structural unemployment problems and overcome the severe erosion of our competitive position stemming from the OPEC induced massive increase in energy, raw material and transportation costs and from the recent sharp reduction in federal corporate taxes.

5. The extension to Puerto Rico, as proposed in the CBI bill, of the 1981 accelerated cost recovery system and investment tax credits and the extension of R & D benefits as major new development tools.

6. A strong federal policy for the development of maritime transportation including ports development, airport and ground transportation infrastructure in Puerto Rico is necessary to be consistent with the Administration's plans under CBI to develop Puerto Rico into a major transportation hub for the Caribbean.

I respectfully submit that it is vital to address and resolve these issues to enable Puerto Rico help itself to achieve economic development and social justice and to enable us to become a major participant and positive force in achieving the Administration's objectives of rapid economic growth, stability and peace in the Caribbean Basin.

ATTACHMENT A

Characteristics of Unequal Treatment and Estimated Additional Federal Assistance in 1979 Had Puerto Rico Been Treated Like a State

Federal Department	Program	How Puerto Rico's treatment differs from States	Estimated additional assistance under Statehood 1/ ($ million)
Education 2/	Elementary and Secondary Education (Title I)	Different allocation formula applied	$ 68
Health and Human Services 2/	Supplemental Security Income (SSI)	Excluded	304
	Aid to Families with Dependent Children and Adult Programs (AFDC)	Federal matching rate set at 75 percent and island funding subject to a ceiling for fiscal year 1979	62
	Social Services (Title XX of Social Security Act)	Instead of being included in the formula, $15 million are set aside for Puerto Rico	24
	Medicaid (Medical Assistance Program-Title XIX of Social Security Act)	Matching rate set at 50 percent and island funding subject to a ceiling in fiscal year 1979	82
Treasury	General Revenue Sharing	Not included	263
Plus:	Earned Income Credit payments (See pp. 128 and 129.)		31
Less:	Projected reduction in Food Stamps due to projected increases in SSI and AFDC payments		(113)
	Total		$721

1/Calculations are described in appendix III. In each case, we consulted Federal officials responsible for administering the programs, and they concurred with the methods for computing estimates.

2/Department of Health, Education, and Welfare in 1979.

Source: General Accounting Office Report to the Congress, Puerto Rico's Political Future: a Divisive Issue with Many Dimensions, March 2, 1981.

Chairman GIBBONS. Thank you, sir.

I am struck by not only the fine quality of your testimony, but what is contained in here about the increases in per capita income from 1950 to 1980. I realize that is a long time and a lot has happened to the value of a dollar, but it went from about $300 a year in 1950 to $3,400 in 1980. And while I realize there has been some serious readjustment during some of these times for some of the industries that you lost—how much higher is the per capita income of Puerto Rico than the rest of the islands surrounding it? Are you familiar with that?

Mr. CORRADA. It is certainly much higher than what you would find in the more immediate islands, such as the Dominican Republic or Haiti, which is still down there in the $260 per capita that we were back on the forties. And of course, it is much higher than the communist model in the Caribbean, Cuba, which is well below that figure in spite of the massive aid poured in by the Soviet Union to Cuba.

But for instance, there are other areas in the Caribbean, such as Trinidad-Tobago, as well as the Bahamas, that currently surpass Puerto Rico in per capita income, mainly given the fact that they have a much smaller population and are highly developed in terms of tourism.

But we feel proud of this achievement, and I must tell you that essentially it relates to three factors: the will of the Puerto Ricans to improve their condition in spite of limited resources; second, a very strong economic development program that brought about investment of capital, mainly from U.S. companies doing business in Puerto Rico, which have promoted very intensively the creation of jobs in the manufacturing sector; and third, the Federal policies of programs to promote health, education, jobs, economic development in Puerto Rico as well as in the rest of the U.S. mainland.

I attribute definitely to those three major elements the reason why we have had that dramatic improvement. Nevertheless, I must point out, Mr. Chairman, that of course that per capita income, high as it is in comparison to Latin America and the Caribbean, still lags behind and is about 50 percent of the State of Mississippi.

Chairman GIBBONS. Yes; now let me ask you, what is the population of Puerto Rico?

Mr. CORRADA. 3.2 million inhabitants.

Chairman GIBBONS. You had the advantage of listening to Mr. de Lugo's presentation about the rebate of the rum excise tax. And as you know and I am sure you recognize the current legislation before us just leaves all of that, with no criteria set, to the Secretary of the Treasury, which would certainly make him a very popular man in the Virgin Islands and in Puerto Rico in having to divide up that money that way with no criteria spelled out as to how he should divide it.

What do you think is the proper division of that rebate of the excise tax?

Mr. CORRADA. Mr. Chairman, of course I have no problem with a provision in the bill setting specifically the formula for that division, rather than allowing the Secretary of the Treasury to do it, although I do not have a major problem with that, either. But I think that it might be the best thing to do to specify that formula in the bill.

And I think, Mr. Chairman, in all due respect, and with the friendship and appreciation that I have for my dear colleague Ron de Lugo from the Virgin Islands, that that division ought to be based on the same proportion that now exists in what Puerto Rico receives from the rebate of excise taxes on Puerto Rican rum and what the Virgin Islands is receiving as a sort of rebate to the Virgin Islands on the production of rum.

That is, the division should reflect the current market that Puerto Rico and the Virgin Islands have in the Unites States, and that proportion should be applied to the rebate of the excise tax on foreign rum. Currently Puerto Rico receives about $242 million in excise taxes and the Virgin Islands about $37 million. It is about a 90–10 proportion, and that is the proportion that I suggest this committee should support.

Chairman GIBBONS. Do you see any trouble with the Puerto Rican rum industry surviving under this? Not the division of the tax, but the other.

Mr. CORRADA. We have had very serious concerns, Mr. Chairman, about this matter, of course. And initially we opposed and told the administration that we would oppose the elimination of the foreign tariff on rum, the duties on foreign rum, because we felt that this could seriously injure the Puerto Rican rum industry. However, in the bill three concessions were made and assurances:

One is that they would rebate to Puerto Rico and the Virgin Islands the excise taxes on foreign rum just as they do the excise taxes on Puerto Rican and Virgin Islands rum;

Second, that the President if, even after that measure, there is a reduction in the revenues collected by Puerto Rico and the Virgin Islands as a result of the elimination of the foreign tariff, that then the President would provide for other measures to compensate Puerto Rico and the Virgin Islands for any loss in revenues;

And third, that if it was determined by the administration that still the Puerto Rican revenues are being affected or that the Puerto Rican economy is being affected by the elimination of duties on foreign rum, that then the President would reimpose the tariff and the duties on the foreign rum.

We have still some concerns with those assurances, but we believe that they do represent an honest, good faith effort on the part of the administration to take into consideration our concerns, and therefore we are supporting this provision of the bill.

However, Mr. Chairman, I must tell you, obviously, that I am open and I am certainly willing to discuss with Ron de Lugo and the Governor of the Virgin Islands this matter, and obviously see if there could be an agreement in terms of additional protection both for Puerto Rico and the Virgin Islands that can be mutually acceptable.

Chairman GIBBONS. Do you have the same problem with the withholding tax outlined by the Virgin Islands? Has that been an issue?

Mr. CORRADA. No, that does not pose a serious problem to us and therefore we are not asking for that.

Chairman GIBBONS. As far as investment is concerned, it is not a serious problem. All right. Well, thank you very much.

Mr. Bailey?

Mr. BAILEY. Thank you, Mr. Chairman.

I would like to welcome the gentleman from Puerto Rico. He is a good friend of mine. I cannot say that I share his reflections on this particular case, at least not at this point.

I would like to ask questions, Mr. Corrada, about the investment tax credit. I think the situation is now that a corporation which has, say an American subsidiary that has a location in Puerto Rico, can elect to make a choice, as I understand it, on the investment tax credit which they can take against their tax liability, or they can elect to become a participant in a certain kind of a tax elective that has to do with Puerto Rican tax liability. And they can, I suppose, choose whichever is most beneficial to them.

The question I have is this: How can the net effect of the Caribbean Basin Initiative be positive for Puerto Rico in terms of the investment that it is going to attract? You know, I started on page 12 and was reading through all these assurances.

One word caught my mind, the word "may." "The President may," in reference to the rum trade, may pull this thing off. Well, we get all kinds of "may's" and all kinds of requests for Presidential authority. I cannot conceive in the middle of the ballgame the President making that change to the benefit of Puerto Rico. As a practical matter, I cannot, no matter how beautifully it is written up as a letter or a commitment, I cannot picture that as a practical matter.

How in the name of goodness can the net effect of these tax advantages help Puerto Rico?

Mr. CORRADA. Don, I share some of your concerns and let me say I think it is important that we see that Congress follows up on many of the assurances given to us by the President in the process of discussion of these matters with his administration.

But let me point out in the specific case of additional incentives, it is not a situation where the President has said that he may do this or may not do that. Those additional tax incentives for Puerto Rico are incorporated in the bill sent by the President here. That is, the additional investment tax credits as well as the accelerated cost recovery system. In other words, they are a part of the package.

Mr. BAILEY. I understand that.

Mr. CORRADA. But we do believe there may be some concern about the possibility of investors, because of this legislation, investing let us say in the Dominican Republic or Jamaica or Haiti or elsewhere in the Caribbean, rather than Puerto Rico. However, we believe that those possibilities are limited, and I will tell you why.

First of all, Puerto Rico has already the provisions contained in Section 936 of the Internal Revenue Code.

Mr. BAILEY. That is what I am talking about.

Mr. CORRADA. Plus these additional incentives that are provided in this bill. And we believe that the power of Puerto Rico to attract—to continue to attract vigorously investment in Puerto Rico vis a vis what potential investors would have elsewhere in the Caribbean as a result of the tax incentives provided in this legislation would retain Puerto Rico's ability to continue to promote vigorously investment of capital in our area.

Second, we believe that, given the fact that Puerto Rico is right there in the middle of the Caribbean, that the economic development and the political stability of those areas, such as the Dominican Republic, Haiti, Jamaica and so on, are a matter of concern to us. In other words, that although there may be certain elements of sacrifice in this legislation for us, we do believe that that sacrifice will be well paid in terms of bringing about economic development to those who live in the Dominican Republic, Jamaica, and so on; and furthermore, that it would curtail the arrival of the illegal immigrants to Puerto Rico from Haiti, the Dominican Republic and all other areas, that further exacerbate our problems of unemployment, simply by promoting the development of these areas.

Furthermore, if these are economically developed we also see potential for trade increase between Puerto Rico and these areas in the Caribbean Basin, so that ultimately these policies should result as well in increased economic activity and in trade exchange between Puerto Rico and other countries.

Mr. BAILEY. Are you satisfied that Puerto Rico or the Administration has sufficiently studied the net impact of the CBI on Puerto Rican investment, that it would increase it rather than decrease it? Because if you are you are the first one to state it.

Mr. CORRADA. Well, in the element of trade I believe, and I suggested in my testimony, that a commodity by commodity analysis, an industry by industry analysis, should be made and the subcommittee should require Ambassador Brock and the Department of Commerce and the ITC to submit information and analysis as to what this policy could do on a commodity by commodity basis. And as a result of those analyses, I would support, if the analyses demonstrate that this policy is going to bring about serious injury to any of those commodities, that further protective measures be taken.

One area we have a great concern for is tuna. Puerto Rico processes 40 percent of the tuna consumed on the U.S. mainland. We are concerned that these policies could result in a weakening of the tuna industry in Puerto Rico by competitors in Costa Rica and Panama that do not have to comply with the kind of standards—wage conditions, salaries, environmental protection—that we have to comply with in Puerto Rico.

And I think these matters ought to be studied by the subcommittee and that there may be the need to determine that in certain specific industries and commodities you should provide either for a phase in of the duty free or to retain some of the duties or quotas.

Mr. BAILEY. Let me say that I know how hard you work. I know you personally. I have served with you on the Education and Labor Committee, and nobody has more respect for you than I do. I hope the people in Puerto Rico understand how hard you work. Nobody can sing your praises more greatly than I could.

I just sincerely hope that we sit down and, instead of the glossed-over view that has been taken concerning this initiative and what it is supposedly going to do, that we do a little bit of homework on exactly what it will accomplish. Let me tell you just a couple of little things that trouble me.

The administration has come to the Senate and they want to make some recommended changes. They are going to come to us and they want an additional alternative minimum corporate tax. Take that and compare it to what they are trying to accomplish with the so-called CBI—I am speaking strictly from the tax structure point of view. I am talking about looking at the investment tax credit, accelerated depreciation, and how they are supposed to apply. Then look at some of these recommendations that they are making about alternative minimum corporate tax, for example, including adding in as a preference item some of the proceeds from so-called safe harbor leasing provisions to that alternative minimum corporate tax.

And somebody says to me that represents a commitment to this kind of tax structure, then we see it show up in the CBI. I have a hard time believing things like this— that there is a commitment to these things. Let me give you a couple of examples.

Think of that tax structure and what it is supposed to mean for industrial reorganization at home, Puerto Rico, the Virgin Islands, the Caribbean Basin. Think how those things are, at least in terms of tax theory and application, to my mind at least, very much in conflict, because American corporations are going to turn around and say that for capital intensive industries in this country, they are going to be kicked while they are down with this alternative minimum corporate tax, while the tax advantages are going to be extended to the Caribbean Basin at the same time.

My honest opinion is, and again I am eyeballing it, that the advantages will not lie, the net advantage will not lie with Puerto Rico or the Virgin Islands. I have a hard time seeing how it could.

Here is an administration commitment that you are after, continuation and strengthening of an adjustment assistance program related to the CBI initiative and establishment of an early warning system to identify threatened industries and plants before they are damaged and to help them become more competitive, produce new products, save and expand jobs.

I do not know exactly what adjustment assistance program means. But if it has anything to do with the attitude toward trade readjustment assistance, I would have to say that I think that promise may be somewhat empty. I do not know what they specifically have in mind.

Strengthening the Federal tax incentive program and supporting such a 936, which is the alternative to the provisions for Puerto Rican industries that you mentioned, and related provisions in the Internal Revenue Code to help ourselves in overcoming our difficult structural unemployment problems and overcome the severe erosion of our competitive position, stemming from the OPEC-induced massive increase in energy, raw material and transportation costs and for a recent sharp reduction in Federal corporate taxes. That goes right back to the point I was mentioning about how the inducements specifically help Puerto Rico.

I honestly do not know yet. I do not know. I hope you are right, I hope they do.

The other points, of course, we have been discussing. With unemployment at 22 percent—and I assume that is based on the assured unemployment rate in Puerto Rico; your real unemployment is probably higher than that. At least in the United States those figures do not really tell the truth.

The thing that really concerns me most is that investment picture, because your economy is more technically involved than are the other Caribbean Basin countries affected by this initiative. I just do not see how it helps your investment, given that structural unemployment problem.

You might get some expansion out of it, but the relative impact I would think would be negative. I just hope you look at it. Many of the things you mention here go back to the New Federalism attitude the administration has, that really have to do with eliminating the very things that you began with in your statement that I happen to agree with you on and would help Puerto Rico.

So I do not know yet. I am very impressed with the details in your statement and the strong position that you took, and it does impress me. I mean that sincerely. But I do not know how much the administration has studied it.

Reading in the briefing book here they talk about the investment potential. I do not know exactly what the minimum losses are going to be or what the net impact in Puerto Rico is going to be.

Mr. **Corrada**. I know about your concern about the possible flight of capital investment from U.S. domestic areas to areas abroad, and I think it is important for us to provide for safeguards against that flight of capital. But I also believe that if later we are going to be in a need to provide military assistance to take care of security problems in the areas, then we are spending our money too late and for the wrong purposes.

I would rather prefer to see a strong policy of the United States in promoting economic development of those areas so that the kind of poverty conditions and political instability situations that result in our later having to get there—not with moneys that we will provide for the creation of jobs and economic development, but money to help a government attempt to suffocate an uprising or a revolution—I think it is the wrong priority.

I firmly believe that this bill is an attempt to put our money where we ought to invest it and to get the kind of return we want.

Mr. **Bailey**. I agree. I think the goals are laudable, and I share them, and I used that same language in reference to the gentleman who was here before you. I just wonder if it will really accomplish that end.

We have invested in other countries, too, but we have not done a doggone thing for the very things you said on that Education and Labor Committee, and that really is where the rubber meets the road.

I hope you are right. I do not know. I am just not convinced yet. I thank you very much.

Thank you, Mr. Chairman.

Mr. **Pease**. Mr. Chairman, I do not have any questions. I would just like to commend my distinguished colleague from the 96th Congress, as well as Mr. de Lugo who preceded him, and the Governor for excellent testimony this morning. I think we have a much clearer understanding of the situation regarding those U.S. territories and possessions. Nobody on this committee wants to do anything intentionally which will hurt U.S. citizens in those territories, so we need to have this information; and we are indebted to our colleagues for giving it to us this morning.

Mr. CORRADA. Thank you.

Chairman GIBBONS. Thank you, sir.

Mr. CORRADA. I would like to add before I conclude that you will be tomorrow listening to testimony of other people who will come from Puerto Rico. And I would like to point out that my recommendations, as well as others, should address the practical considerations to protect Puerto Rico and the Virgin Islands in this legislation.

I do not believe that this hearing should turn out to be a debate about the future political status of Puerto Rico or changes in the political status of Puerto Rico. As you very well know, I support statehood for Puerto Rico. I believe under the Commonwealth we are second-class citizens. We do not vote for the President of the United States. We do not have six voting Congressmen and two Senators, and I believe we do not have equal treatment in a number of Federal programs for Puerto Rico that I would certainly want to see us have. And that is an ongoing debate in Puerto Rico.

But I do not think this subcommittee should get into the question of should we support policies related to retaining the present Commonwealth relationship, should we support policies to move Puerto Rico toward independence, or, as we will hear tomorrow from Commonwealth supporters, asking Puerto Rico be given the right to impose their own tariffs, to enter into agreements with foreign nations on matters pertaining to trade and commerce, and even to impose restrictions or limitations on the goods and articles that can be shipped from the U.S. mainland to Puerto Rico, which are suggestions that may sound very demagogic and very attractive to our local people down there. But, Mr. Chairman, if we are part of the U.S. domestic market and our products have free access to the U.S. mainland without any kind of restriction, and there is a considerable degree of exchange between the United States and Puerto Rico, how can we want to have the cake and eat it, too? I mean how do we want to be part of that same U.S. domestic market, have the benefits of access to that market, have the benefit of Federal programs for housing, education, food stamps, and so on, and then come here and say give us the right to impose our own tariffs.

I am sure that Chairman Gibbons would like Florida to be able to protect itself with its own tariffs from importation from the Caribbean. And Bill Brodhead in Michigan, and Don Pease in Ohio, and Don Bailey in Pennsylvania would certainly want their States to be able to negotiate with foreign countries. And it would sound great, but the point is this: If we are part of the same common market and the common market with the United States, is not only a pillar under potential statehood; it is an essential element in the current Commonwealth relationship.

Then, Mr. Chairman, we have to be careful that we do not come here grandstanding to support all these rights for Puerto Rico while from the other side of the mouth we are asking for more Federal funds to support us there.

I want to warn you because tomorrow you may be listening to that kind of testimony. And I hope, Mr. Chairman, that you will not allow these hearings to become a forum for the debate of Puerto Rico's political status, because we can take care of that in the House Interior Committee at the time the matter is addressed by our people.

Chairman **GIBBONS**. Thank you for your observation.

I agree that this is not the proper forum for that debate. Speaking personally, Puerto Rican people can do whatever they want to in their own free will. I would not even try to prescribe what would happen in case they wanted to change; but whatever change they want to make of course is up to them as far as I am concerned.

I have often looked at the status of Puerto Rico, and I frankly would be hard-pressed to describe a status that is more advantageous than the status is right now for Puerto Ricans, although I realize I do not see the problem as closely nor perhaps as accurately as do other people in Puerto Rico, but I am willing to listen to them and declare my personal position to be they can do whatever they want to as far as independence or statehood or maintaining the current status.

Thank you, sir.

Mr. **CORRADA**. Thank you, Mr. Chairman, for your time. Thank you.

Chairman **GIBBONS**. Our next witness is our former colleague, the former resident commissioner of Puerto Rico, Mr. Jaime Benitez.

We remember you fondly, we welcome you here, and your entire statement will be a part of the record. You may proceed as you wish.

STATEMENT OF JAIME BENITEZ, FORMER RESIDENT COMMISSIONER OF PUERTO RICO

Mr. **BENITEZ**. Thank you, Mr. Chairman.

My name is Jaime Benitez, and I appear before this subcommittee in my individual capacity as a concerned citizen and as a member of the constitutional convention of Puerto Rico, the main contracting body with the 81st and the 82nd Congress for the creation of commonwealth status for Puerto Rico.

In spite of the anticipatory reply that we have just heard from the Resident Commissioner concerning status, the awful thing about this proposal is that it is one where status is injected by the President of the United States, and it is one wherein unfortunately, as well as indicated by Mr. Bailey earlier, the whole political international issue pertaining to the Caribbean and even to America is involved with a number of trade proposals, all of which basically are intertwined with very serious and grievous aspects concerning Puerto Rico and Puerto Rico's Commonwealth.

I may read briefly from the fact sheet sent by the State Department to you where specific reference is made to a series of measures, page 4 of the fact sheet, "will support the efforts of Puerto Rico and the Virgin Islands to play a dynamic role in the Caribbean region; for example, involvement of the possessions will be critical."

The basic fact is that this Congress and the people of Puerto Rico many years back, 30 years back, repudiated that terminology, and it is passing strange that the State Department, presumably responsible for looking after the interests and the good name of the United States, should feel at liberty to refer to the Commonwealth of Puerto Rico as a possession of the United States.

So I come here to defend that status against its adversaries here, foreign and domestic. That defense is particularly relevant in light of several adverse consequences to Puerto Rico resulting from the Caribbean Basin Initiative presently under consideration.

I just want to make one basic point, and the whole thing my testimony deals with is one basic point. I have no doubt that it is in the general interest of the United States or of Puerto Rico, of the Virgin Islands that the Caribbean Basin be stabilized at the earliest possible time. But in working toward that goal we cannot forget the role of Puerto Rico within the Caribbean with reference to the United States and to the rest of the communities. If as a result of the progress toward Caribbean stabilization Puerto Rico itself is destabilized, you may be certain that all other efforts of the United States will go for naught.

Chairman **Gibbons**. Excuse me. Let me make an administrative announcement.

We have got a vote on, and what I had planned to do is to recess right after your testimony and reconvene about 1:15. So those of you who are waiting to testify, we will take no more witnesses until 1:15.

Mr. **Benitez**. Mr. Chairman, if it is to the advantage of the committee to recess now, I can resume in my testimony.

Chairman **Gibbons**. How much longer do you think it will take? I have read your statement here.

Mr. **Benitez**. I am not going to read it all.

Chairman **Gibbons**. OK. Let us go as far as we can and see how it comes out.

Mr. **Benitez**. At any time it is necessary for you, I am perfectly well aware after 4 years of working here——

Chairman **Gibbons**. Go right ahead.

Mr. **Benitez**. Now, I must add this, that the success or failure in the case of Puerto Rico is indicative more than any place else of the image and the role of the United States in the Caribbean, and I must add this, very frankly and very honestly to all of you, I have never in the last 40 years seen greater concern and perturbation in Puerto Rico with American policies than those that have resulted from the New Federalism, not from the cuts, but from the attitude toward the poor and the educational activities and also in this particular initiative.

So I must also say that since President Reagan has announced his support of statehood for Puerto Rico subject to ratification, well, Fidel Castro has long been an activist for independence despite Puerto Rico's opposition. I wish to clarify from the start that Puerto Rico at every past and present electoral test has rejected both independence and statehood. I daresay we will continue to do that for the foreseeable future.

I must say that the present status which the Congress of the United States and the President of the United States after a prolonged period of 4 years—discussions, debates, arrangements—agreed on the free associated state called Puerto Rico. We have fundamentally achieved what later was accepted both by the

Public Law 600 of 1950 and the Constitutional Convention as a relationship "in the nature of a compact" by mutual consent, which is the basis of our union with the United States of America.

I think, Mr. Chairman——

Chairman **Gibbons**. Let me ask you a question before we recess here. Do you have any specific changes you want us to make?

Mr. **Benitez**. Yes, sir. I will be making some recommendations.

Chairman **Gibbons**. Go right ahead.

Mr. **Benitez**. I would much prefer, Mr. Chairman, if you would recess at this point, and we can talk perhaps with a little bit of greater leisure and without the immediate——

Chairman **Gibbons**. Well, I notice on page 9 of your statement you recommend some changes. Are those the changes you want to discuss?

Mr. **Benitez**. No, sir.

Chairman **Gibbons**. Where are they in your statement?

Mr. **Benitez**. The changes I want to discuss basically —I want to discuss all of them. I might say I made this trip here just for this purpose. Aside from that, the ones I would mainly wish to discuss are the ones covered on page 9 on——

Chairman **Gibbons**. That is what I was referring to, yes. All right.

Well, we will reconvene then at 1:15, and we will discuss those items on page 9.

[The prepared statement follows:]

STATEMENT OF JAIME BENITEZ,* PROFESSOR OF GOVERNMENT AT INTERAMERICAN UNIVERSITY

My name is Jaime Benitez, I appear before this Subcommittee as a member of the Constitutional Convention of Puerto Rico, the main contracting body with the 81st and the 82nd Congress for the creation of Commonwealth Status for Puerto Rico. I come to defend that status against its adversaries, foreign and domestic. That defense is particularly relevant in the light of several adverse consequenes to Puerto Rico resulting from the Caribbean Basin Initiative presently under consideration before the 97th Congress.

I wish to make one basic point. I have no doubt that it is the general interest of the United States that the Caribbean Basin be stabilizd at the earliest possible time. But in working towards that goal, we cannot foreget the role of Puerto Rico within the Caribbean with reference to the United States and to the rest of the communities. If, as a result of the progress towards Caribbean Basin stabilization Puerto Rico iteself is de-stabilized, you may be certain that all other efforts of the United States will go for naught. For after 84 years of intense relationship, Puerto Rico, more than any other place in that area is indicative of success or failure of the United States in dealing with a Caribbean community. I must add that since the 30's I have never seen a greater concern in Puerto Rico towards American policies than at this juncture.

Since President Reagan has announced his support of statehood for Puerto Rico, subject to our ratification while President Fidel Castro has long been an activist for independence, despite Puerto Rico's opposition, I wish to clarify from the start that Puerto Rico at every past and present electoral test has rejected both Statehood and Independence. I dare say we will continue to do that for all forseeable future.

It is not that we dislike the United States and, therefore, oppose incorporation. Nor is it that we fear freedom and therefore reject separation. It is quite the opposite on both counts. After half a century of ups and downs in our relationship, we have discovered that we can live in permanent association with the United States best and can achieve our own collective and individual freedom most meaningfully through a free, lasting, autonomous relationnship.

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*Testimony rendered by Jaime Benitez, Professor of Government at Inter-American University, Resident Commissioner for Puerto Rico in Congress 1972-1976, President and Chancellor of the University of Puerto Rico 1942-1971.

We can be true to our own selves best and loyal to our common democratic destiny most effectively by agreeing upon a mutually far-sighted, flexible relation. Our Constitutional Convention designated that relationship in Spanish as Estado Libre Asociado. The Congress accepted the Spanish form which, following the Anglo-American traditions, was rendered as Commonwealth in English.

On the 25th of July 1952, exactly 54 years to the day when American troops landed in Puerto Rico at the end of the Spanish-American War, we jointly resolved to end colonialism in Puerto Rico. After four yers of negotiations involving the Congress and President of the United States on one side and on the other the Governor, the Legislature, the Constitutional Convention and the electorate of Puerto Rico, the new status was proclaimed. To quote both the text of Public Law 600 of 1950 and the Constitutional Convention of 1952, the relationship was established "in the nature of a Compact", "by mutual consent which is the basis of our union with the United States of America".

On November 27, 1953, the General Assembly of the United Nations approved its Resolution 748 (VIII), which states in part that:

Considering that the agreement reached by the United States of America and the Commonwealth of Puerto Rico, in forming a political association which respects the individuality and the cultural characteristics of Puerto Rico, maintains the spiritual bonds between Puerto Rico and Latin America and constitutes a link in continental solidarity,

* * * * * * *

2. Recognizes that the people of the Commonwealth of Puerto Rico, by expressing their will in a free and democratic way, have achieved a new constitutional status;

3. Expresses the opinion that it stems from the documentation provided that the Associaton of the Commonwealth of Puerto Rico with the United States of America has been established as a mutually agreed association;

4. Recognizes that, when choosing constitutional and international status, the people of the Commonwealth of Puerto Rico have effectively exercised their right to self-determination;

5. Recognizes that, in the framework of their Constitution and of the compact agreed upon with the United States of America, the people of the Commonwealth of Puerto Rico have been invested with attributes of political sovereignty which clearly identify the status of self-government attained by the Puerto Rican people as that of an autonomous political entity;

* * * * * * *

9. Expresses its assurance that, in accordance with the spirit of the present resolution, the ideals embodied in the Charter of the United Nations, the traditions of the people of the United States of America and the political advancement attained by the people of Puerto Rico, due regard will be paid to the will of both the Puerto Rican and American peoples in the conduct of their relations under their present legal statute, and also in the eventuality that either of the parties to the mutually agreed association may desire any change in the terms of this association.

Shortly thereafter, Earl Warren, at the time Chief Justice of the Supreme Court, described Commonwealth as "the greatest American innovation of the century in political theory".

During the 50's and 60's Commonwealth continued to flourish. Upon the recommendation of a Joint U.S.-P.R. Status Commission—created under both Congressional and Legislative Resolutions—a status plebiscite was held on July 27, 1967. The retention and improvement of Commonwealth status was endorsed by 60 percent of the electorate. Unfortunately, neither President Nixon, nor President Ford, nor the Congress ever acted upon that plebiscite. Pursuant to it and after three years of studies, hearings and deliberations, a new compact was drafted and endorsed by a 14-member Joint Committee. Among others, the Committee included Thomas Foley and Donald Clausen from the House of Representatives, Senator Bennett Johnston and former Senators Marlow Cooke, who presided over the American delegation and James Buckley. Puerto Rico's delgation was presided over by Luis Munoz Marin. I was honored as its Vice-President.

President Ford pocketed the unanimous commendation for 15 months. After his own defeat, he submitted to Congress instead a pro-statehood bill. It got nowhere. In the meanwhile, the Subcommittee on Territorial and Insular Affairs, presided over by Phillip Burton, had approved on August 23, 1976, with minor modifications, the recommendation for a new compact.

After the oil crisis of 1974, the Pro-Commonwealth Government, then in power, like most other governments in democratic communities affected adversely by the crisis, went to defeat, on the general elections of 1976, exclusively on economic and administrative considerations. In the November 1980 election it recovered enough to regain control of both Houses and of 54 out of 78 municipalities. But it lost both the post of Governor and that of Resident Commissioners by a very small margin to Pro-Statehood advocates.

It is against this background that I, as one present at its creation and involved in its future, appear before this Subcommittee to raise three basic issues concerning President Reagan's proposed Caribbean Basin Initiative, insofar as it affects Puerto Rico and its Commonwealth status.

1. Unless substantially amended, the proposal will not significantly help the Caribbean Basin, if at all. At the same time, it would radically harm Puerto Rico and the Virgin Islands.

2. The international, as well as the economic implications of the proposal, makes it advisable that, regardless of its operational amendments, other members of the larger American community like Mexico, Venezuela, Costa Rica, Canada, perhaps the Organization of American States itself, participate in the formulation and supervision of an overall Caribbean Commission assigned to deal with and to participate in the working of any such Caribbean organization. Both Puerto Rico and the Virgin Islands should be invited to become active members in such a Commission.

3. In any case, both Puerto Rico and the Virgin Islands require specific economic safeguards beyond those alluded to generally in President Reagan's proposal.

I will not expand upon points 1 and 2 unless requested. Neither will I presume to speak for the Virgin Islands. But as a deeply concerned citizen of the United States and as a proud member of the Commonwealth of Puerto Rico I wish to state briefly the following with reference to point 3:

We have no objections to the well-being, the social advancement and the democratic strengthening of each and all members of the Caribbean. On the contrary. It is true that the free trade offered to them now and the tax holiday offered to American investors and to the profits resulting from their investments in other Caribbean communities served Puerto Rico well when made extensive to us under Commonwealth. But it must be underscored that the program which to be known everywhere as Operation Bootstrap would have hurt us rather than helped us had it not been preceded by a most extraordinary ten-year period of internal decolonization. That internal decolonization was for us an essential prerequisite to everything that followed.

The extraordinary 10-year period oftentimes described as Puerto Rico's peaceful revolution was basic to the fundamental transformation of a community which President Hoover had called in 1929 "the poor-house of the Caribbean" and which years later would be called—overenthusiastically—"the show-cáse of the Caribbean".

Puerto Rico's internal decolonization began on the 5th of November 1940 with the unexpected electoral triumph of the Popular Democratic Party under the inspired leadership Luis Munoz Marin. It was a most effective and dramatic campaign for long denied social justice which was to be achieved upon the basis of an electorate mandate. The mandate was followed shortly by the advent to local public responsibility of a strong, competent, socially oriented government embued with the highest ethics of public service, committed to the rehabilitation of Puerto Rico. That program was buttressed for the next twenty years by full electoral support.

A wide-ranging program of public and private initiative was developed. It fostered health, education, employment opportunity for all. Public attention was focused on the social, economic, cultural evils attaching to centuries of colonial helplessness and of metropolitan benign neglect.

In October 1941 we were most fortunate in that, after forty years of mediocre, shortsighted or incompetent chief-executives, the last appointment of a non-Puerto Rican governor was made by President Franklin D. Roosevelt. He named the devoted, courageous and exceptionally able administrator Rexford G. Tugwell. For five years, he collaborated fully with the new program and with its leader, Luis Munoz Marin.

Thanks to a large degree to the meeting of those two great minds, Munoz Marin and Tugwell, each representing the best traditions and ideals respectively of Puerto Rico and of the United States, we achieved a very remarkable take-off towards political self-fulfillment. We moved in that direction not against, but in cooperation with, the United States.

Up to 1940, many of us who had been educated in the best American universities had regretfully come to the conclusion, based on first-hand knowledge of Puerto

Rican realities, that for all its great achievements in the field of democracy, the United States Government was somehow incapable of carrying its best traditions beyond its continental shores. After ten years of intensive cooperation in war and in peace—from 1941 to 1951—we were resolved now to advance a new experience of understanding and mutual assistance for all years ahead. Commonwealth status was the result.

Commonwealth status in now under severe attack in Puerto Rico, in Washington, in Cuba, and in the Soviet Union. In spite of the climate of disillusionment which afflicts mankind everywhere, we hold firm to the conviction that cooperation, understanding and mutual respect are preferable to violence, to dictatorship, to minority rule, and to colonialism in any of its forms.

Commonwealth status, incomplete as it is at present, represents, nontheless, a potentially fruitful contribution towards a future of indispensable, plural and democratic alternatives. It aims at affording a common ground of lasting values, goals and interests between the strong and the weak, the rich and the poor, the underdeveloped and the overdeveloped.

Both the United States and Puerto Rico must facilitate the growth of the Commonwealth. Let us not destroy, even inadvertently, this new, vital, endangered species. The tragic irony of the proposal in its present form is that it inivites others to profit from the past achievements of the Commonwealth of Puerto Rico and, in so doing, nullifies the further development of Commonwealth itself.

With reference to possible amendments, I wish to support the following:

1. The safeguards recommended early in the year to the President's Trade Policy Committee by the Honorable Miguel Hernandez Agosto, President of the Senate of Puerto Rico. Those safeguards represent workable improvements upon the original proposal. If the plan is to be followed, these balancing measures should be approved.

2. Additional powers will be requested tomorrow by the Legislature of Puerto Rico concerning trade, shipping, immigration and special arrangements within the Caribbean Basin. They were already embodied in the New Compact to which reference was made earlier. In 1976, we meant to achieve exactly the same purposes that render them indispensable now in the light of the President's proposal.

3. More directly relevant to Puerto Rico's present plight is a proposal that has been doing the rounds informally here in Washington and in San Juan, and which, I think, will be given most serious consideration at both places. It aims to put together the main conclusions of the three-year economic study of federal assistance to Puerto Rico undertaken at President Carter's request, known generally as the Kreps Report. The proposal relates them to the impact of both the New Federalism and the Caribbean Basin Initiative and endeavors to provide a highly promising general approach.

I quote directly now:

"*The New Federalism and Puerto Rico*—The Federal budget cuts in 1981, the prospective cuts in 1982 and later, the uncertainty connected with Federal tax policy as it relates to Puerto Rico, and the Caribbean Basin Initiative (which dilutes the special treatment extended to Puerto Rico in its historical relationship to the U.S.) have created an atmosphere of distrust on the Island toward the Administration.

* * * * * * *

"Psychologically the Island is floundering with every rumor of change in Federal policy creating political pressures on the system. A cyclical upturn of the mainland economy would dampen some of the fears—increased capacity utilization should restore some employment—but the structural aspects of the investment slowdown (related to the above cost factor) and Federal budget cutbacks will probably maintain for the foreseeable future unemployment at levels not seen since the recession of 1974–1975.

"Economic policies on the Island are substantially dependent on exogenous factors. Few of these factors are influenced by the realities of the Island. Therefore, sustainable growth is questionable over the medium-term. One possible solution is that large numbers of people will emigrate to the mainland to seek employment. These emigrants would most likely be bilingual and skilled individuals leaving many unskilled, Spanish-speaking people on the Island, frustrated by the lack of sustainable growth and employment. This frustration could translate into violence or, more likely, efforts in the U.N. and other fora to seek independence. A negative attitude toward the U.S. would reduce our ability to secure national security goals in the Caribbean—closing Roosevelt Roads to the Navy, removing other military installations, and creating a political environment conducive to anti-American blandishments.

* * * * * * *

"* * * In Puerto Rico's case, the New Federalism offers a dramatic opportunity to refocus Federal budgetary policies toward economic development, while obtaining a positive psychological thrust for increasing Island policy flexibility and the potential for a long-term resolution of the status issue.

"I. *Objective of Proposal.*—In the long term (about 20 years) the relationship between the U.S. and Puerto Rico must be placed on the footing of equality, otherwise, the present tensions will become irreconcilable differences that could translate into anti-Americanism and the loss of another friend in the Caribbean.

"II. *Purpose of Proposal.*—The purpose of this approach is to turn the present political/economic impasse in Puerto Rico into a dynamic process of economic development. In the period proposed (approximately 20 years) the energies of the Puerto Rican people could be turned toward creating an economic structure less dependent on Federal resources and special policy treatment (e.g. Federal tax exemption for U.S. subsidiaries in Puerto Rico). The economic restructuring should lead to greater internal savings and investment and increased linkages among the various sectors of the economy. Also, this approach coincides with the Administration's interest in the Caribbean as a whole.

"III. THE PROPOSED APPROACH.—Under the banner of 'The New Federalism' the Administration will seek to increase the Islands's responsibility for development of its economy, while providing the resources and policy flexibility necessary to achieve the desired reduction in the Island's dependence on Federal funds. Specifically, the Administration will establish an entitlement program of about $2 billion (in 1982 dollars) to be used for economic development and economic well-being projects. This fund would replace the present structure of Federal disbursements on the Island, except for Social Security, Medicaid/Medicare, V.A. benefits, Federal Retirement, and necessary Federal agency expenditures. Presently, the Federal Government disburses approximately $4 billion on the Island of which about $1.7 billion is for the above enumerated programs. The remainder $2.3 billion would be reduced by $300 million and subsequent increases in the fund would only result from inflation. This program would continue for 20 years starting in 1984 in this form. At the end of 20 years the Federal tax exemption (Sec. 936) would be terminated for new investment and the Funding mechanism would be modified by the Federal Congress to reflect current concerns and Puerto Rican needs.

"The energy and inventiveness of the Puerto Rican people must be turned-on in order for the Island and mainland to extricate themselves from the present no-win confrontational environment that appears to be an increasing part of the relationship. The responsibility envisioned for the Island will not be without risk, but the alternative is leading toward an irreconcilable chasm governed by misperceptions (welfarism, racism, etc.) on the mainland and on the Island perceptions of indiffence, hostility, and condescension emanating from the mainland. This atmosphere is not in the best interest of the United States nor Puerto Rico."

I am not asking this Committee or even this Congress to act upon these suggestions. The points raised herein go far beyond the possibilities of unilateral enactments. What I am bringing before you are critical issues which cannot be foreclosed if we are going to think and to act with due responsibility towards both the immediate and the long-term future.

[Whereupon, at 12:10 p.m., the hearing was adjourned, to be reconvened at 1:15 p.m., the same day.]

AFTERNOON SESSION

Chairman **GIBBONS**. All right, our hearing will resume.

Mr. Benitez, I am very sorry we got interrupted here by the quorum call, but you are familiar with those kinds of problems. Go right ahead now.

Mr. **BENITEZ**. Thank you.

The main thrust of my paper I think can be briefly summarized by saying that, while I am perfectly well aware that many of the things that are included in this paper are tangential to the specific bill which is up for your consideration, yet the subject itself is one that goes to the heart of our particular relations with the United States, which are ones of permanent association.

Under this system we have achieved a great development. We have advanced significantly in many fields, and the tragic irony of this proposal—not necessarily the one before you, but the whole speech of the President, of which this is just a part, the speech made on February 24—endeavors to transfer to the rest of the Caribbean Basin a number of prerogatives that heretofore had been exclusively for Puerto Rico.

And we do not want to harm anyone, but we do insist that: (A), the reason why we were able to achieve an extraordinary development was because we had set the basis for a strong, competent, able government, which unfortunately is not the case throughout the Caribbean; and that we had worked at for 10 years our form of government, which is indispensable for the success of this operation of private investments, because otherwise the local government lacks the maturity, the experience, the wisdom, to be able to control and to direct and to orient the planning of the society out of a feudal—into a democratic system.

Now, this is not the case throughout the Caribbean, and so the things that have been successful in Puerto Rico are going to be translated to all the communities where they cannot be adequately, properly handled.

And coming to page 9, as the chairman had suggested, I will briefly direct myself to the three main points which are here made. I certainly do not want to anticipate what the legislature of Puerto Rico and the many groups in the legislature of Puerto Rico are going to say to you.

You must realize that Puerto Rico has a divided government at present, where one branch controls the legislature, the house and the senate, and this is the group that believes and fosters the Commonwealth, and the group that believes in statehood won by 3,000 votes or so—the number was very small—both the Governor and the Resident Commissioner.

So when it is said that these matters have been consulted with Puerto Rico, the point is that they have not been consulted with the Legislature of Puerto Rico, nor with the three-fourths of the municipalities which presently are controlled by the Commonwealth group. And while I am not trying to involve myself in this kind of a debate, I do feel compelled as a citizen and as one who participated in much of the work of the constitutional convention to express my conviction that it is wrong to ignore the basic structures that exist in Puerto Rico or to ignore the meaning, the potentiality, the exigencies of Commonwealth.

So I will go to my third point, which refers to the safeguards that were asked for and requested and not granted by the president of the Senate of Puerto Rico, which are embodied in this document. And tomorrow when the legislature for the first time, I think, that I can recall in 30 years asks to be heard—it is not the best place to be heard, I agree, in the Committee on Ways and Means under this bill, but they want to be heard someplace by the Congress and this is the first opportunity that they have.

Now, I note something else which I think is much more important and which in my judgment really tackles this situation, and it is the result of a 3-year study that was made at the request of President Carter concerning Federal funds and assistances to Puerto Rico. The basic conclusion was that these things were necessary under the circumstances and were part of the overall consequences of having to cushion evil days everywhere yet it was preferable that these assistances then had no lasting consequences.

And recently out of that, when I testified when I was a Congressman or immediately after I had left, and I suggested that all these funds could very well be used, at least 50 percent of them, to carry into effect a project, which my then colleague Gus Hawkins and my dear friend Senator Humphrey had prepared for full employment. To talk about full employment now sounds almost like a joke.

But we believed that in Puerto Rico in the past we had been able to formulate programs of social, economic, institutional reconstruction, and that at least half of this money could be devoted over a 10- or 15-year period to carry out a program of stimulation of public and private initiative.

I worked on the plan for that purpose 6 years ago, which would bring back the dynamics, the thrust, the enthusiasm, the goals that are presently lacking, and that it would be much better if, instead of having to react to a Caribbean Basin Initiative, we could parallel it to formulate, develop, organize a new program to get ourselves back on our own feet and for a moment forgo all these debates about status, none of which can be solved, really, as long as we are in our present economic situation; work on these things for 15 years and then come to a final decision, which I hope everybody would be in a position to support.

Chairman GIBBONS. Mr. Benitez, we thank you.

The bell has rung and I must go vote. We will continue this discussion when the legislature is here tomorrow.

Our next witnesses will be from the Caribbean Central American Action, and we will resume after the vote.

[Recess.]

Chairman GIBBONS. We are ready to begin.

Our next group of witnesses are from the Caribbean Central American Action, Peter Johnson and Sam Segnar.

Gentlemen, you may proceed.

STATEMENT OF PETER JOHNSON, EXECUTIVE DIRECTOR, CARIBBEAN CENTRAL AMERICAN ACTION

Mr. JOHNSON. Thank you, Mr. Chairman.

My name is Peter Johnson, executive director of the Caribbean Central American Action, which is a nonprofit organization supported entirely by some 50 to 60 American firms, all of which are in one way or another involved with the Caribbean Basin. The organization is dedicated to the proposition of development through the tapping of private sector resources in the United States and the Caribbean.

I will just make a couple of comments verbally and submit the written statement for the record.

Chairman GIBBONS. Your statement as well as the others will be in the record in full.

Mr. JOHNSON. The points I would like to make are very few, which concern the societies of the Caribbean, and these points might help us to appreciate better that this administration's bill is exactly the prescription to the economic ills affecting these small companies.

While the bill, as we see it, is not a quick fix, it does go to the heart of the problem by providing economic opportunity. I am not a trade expert but I do know something about the Caribbean.

Over the past 7 or 8 years the Caribbean Islands, in particular, were experimenting very seriously with various types of socialism and Marxism. In the last part of this decade the pendulum has swung very sharply to the center, characterized by the election of the new Prime Ministers of Jamaica, St. Kitts and several others.

This new political leadership has been given an opportunity through the democratic system to perform for their populations. The climate for the approach to private development that they are propounding is very strong. That is, it is a positive investment climate, a positive trade climate, a very positive attitude reflected through these populations toward the United States. This is a striking shift from what we saw several years ago in many of these countries.

The Caribbean Basin Initiative responds to what this new wave of political leadership has been asking for. It corresponds precisely to the kind of campaign promises and philosophical approaches that this political leadership has propounded.

The shift in the Caribbean, while quite accidental, corresponds in a very interesting way to a shift that has occurred in the United States. If these political leaders in the Caribbean are going to succeed and if the moderation they represent is going to continue and the relationships that they seek with the United States are going to be strengthened, it is up to the United States itself to be responsive and to play the kind of ball that will make things happen that are in our interest.

The ball is in our court. The political leadership is looking to the United States for the kinds of investment, the kind of trade that will allow enterprise in the Caribbean to prosper and to work for these populations.

I would like to say three things about the bill itself that you all are considering. Once passed, this bill is an opportunity and a medium- and long-term solution to some very serious economic problems. The bill itself will not be self-executing. Since we are talking by and large about countries of 100,000 and 150,000 population with very fragile economies, nonviable economies in many instances, there is going to have to be kind of a promotional effort made to acquaint those hundreds of thousands of middle-sized American businesses with some of these opportunities.

My organization, among others, is dedicated to this promotion, dedicated to making American business aware of opportunities in the Caribbean.

Another area that is going to have to be dealt with rather quickly is to enable these countries to acquire certain elements of primary infrastructure that will in turn permit them to take advantage of some of these opportunities presented in the CBI. I would mention only briefly that in the case of a country like Dominica, a country of 40 percent unemployment, with some very serious economic problems, very small and relatively inexpensive pieces of infrastructure would permit their private sectors to perform in such a way as to take advantage of this opportunity.

Third, the private sectors themselves organizationally in the Caribbean are weak. A good deal of work needs to be done, and we are doing some, to strengthen these private sectors. We have linked in U.S. chambers of commerce with the idea of them sharing their professional expertise with these chambers, and that is functioning.

In sum and in finishing, I feel very strongly that it is in our interest as well as it is in theirs that the CBI pass and mechanisms be established to see that it is implemented as fast as possible.

Thank you.

[The prepared statement follows:]

STATEMENT OF PETER B. JOHNSON, EXECUTIVE DIRECTOR, CARIBBEAN/CENTRAL AMERICAN ACTION

I would like to restrict my comments to the fundamental elements of the U.S. government proposal for the Caribbean Basin. The issue of whether the Caribbean Basin is the proper frame of reference, whether this geographically proximate set of countries has economic points of commonality, or whether the political turmoil affecting some countries on the western side of the Caribbean Basin distorts consideration within this framework are issues addressed by other witnesses.

The fundamental point that we must recognize is that the entire region faces severe economic problems, that these countries are too small and too dependent upon one another and the nearby larger countries to solve their own problems, and that our own security interests are ill served by continued high rates of unemployment and economic underdevelopment. If we can, through enlightened and encouraging trade and investment policies, stimulate private sector growth and increased economic vitality, these largely democratic societies can begin to solve their own problems through the efforts of their own enterprise.

I would like to make several points about the economies and societies of the Caribbean that will help us appreciate that the Administration's bill is exactly the prescription to the economic ills affecting these small countries. While this bill is not a quick fix it does go the heart of the problem by providing economic opportunity. There are also some things that can be done by our government, working in close concert with the U.S. private sector, that can accelerate the implementation process so that its impact can be felt in time to preserve and enhance the stability of the moderate political leadership trend across the Caribbean.

While these points hold true largely in the island Caribbean, I would call your attention to the recent elections in both Honduras and Costa Rica, and the new consensus pulling for private sector emphasis in Panama. We tend to overlook these positive phenomena when our attentions are focused on the volatile political situations in a very few.

1. *The climate for active U.S. involvement in enterprise-oriented development is extremely positive.* During the 1970's many of the countries explored or experimented with forms of socialism or disengagement from the West, while others followed an approach emphasizing private sector growth and close U.S. ties. The contest took place in the context of democratic political institutions. For all practical purposes, the contest is over—at least for a while, while the winners have their turn to perform. Elections all across the Caribbean have brought or returned to power governments emphasizing the U.S.-oriented, enterprise-oriented road to development. In the process the democratic institutions themselves have been vindicated and strengthened. It is critical that we recognize this upbeat trend and the unexpected opportunity it presents. If we approach the region defensively, as if we have to sell reluctant takers on the merits of this development strategy, or if we fail to respond in a sufficiently supportive way, the United States will be in the internationally embarrassing position of refusing to take "yes" for an answer.

2. *The shift toward a private-sector strategy is taking a place simultaneously in the U.S., in the countries themselves, and in multilateral institutions.* The electral shift

in the region dovetails with current directions in U.S. policy as well as a striking shift in institutions like the World Bank and CDB in the direction of private-sector stimulation. This is occurring not in response to political pressures among the various players but a discovery at various levels that alternative approaches alone have not worked, and this might be the missing ingredient.

3. *The shift has occurred at least in part because the U.S. did not force it.* Jamaica and other countries that have turned back from a socialist direction did so for practical internal reasons reflecting the people's judgment about what type of policies could best meet their economic and political needs. The international agencies are moving in the same direction also because of pragmatic judgments about what will get the job done. These moves have not occurred as a favor to the U.S., and indeed could probably only occur in an environment where the U.S. is prepared to live with a diversity of directions and therefore the choice of a direction we happen to favor can be made without arousing ideological suspicions of subservience to U.S. wishes.

4. *The ball is now in our court.* Political leaders who came to power on a platform promising better economic opportunity as a result of closer cooperation with the U.S. and with private business will not maintain their constituencies unless significant performance occurs quickly. While their govering mandates are broadbased, they are also fragile. Nearly every country has a small minority of actively committed marxist ideologues. They also have large swing votes in their electorates willing to give the Western approach a try. Even the commitment to the democratic processes themselves, while deeply rooted historically in many cases, is subject to the potentially ravaging effects of economic despair or polarization over sensitive issues like the maintenance of genuine independence and sovereignty. All this adds up to a very short window in time for the United States to come up with the supportive and responsive policies that produce the kind of economic results that will permit sympathetic leaders to keep their nations on a positive course.

5. *Enterprise-oriented development in the Caribbean does not mean an emasculated public sector.* We have to recognize that a broad consensus in the region exists, based on very legitimate practical considerations, for a much more active involvement of the state in the economy that we would find appropriate in our country. This extends to Seaga's Jamaica and other nations viewed as part of a "conservative trend" the nature of which should not be misunderstood by applying our own domestic uses of the term. Even Puerto Rico, the classic case of the free-enterprise model, is by any standards a mixed economy with a strong leadership role for the government. Our own aid strategy should not be predicated on the expectation that Caribbean governments which are in agreement with step back and let foreign investors plan their economic future. Rather, our efforts must be directed at least in part toward strengthening the capacity of those governments to play the leadership role expected of them in defining, attracting, and working in partnership with the type of investors needed to support their development goals.

6. *Finally, an enterprise-oriented development strategy in no way can suggest a passive role for the U.S. government.* What we are talking about is not a belief that a free market will automatically meet the development needs of the Caribbean, but rather an active strategy by the U.S. Government to stimulate private sector resources—in the U.S. and in the recipient countries—as the primary vehicle for economic growth. This requires at least as much planning and creativity—and probably at least as much public-sector funding—as an approach based on public sector provision of services. It involves transfers of U.S. official assistance both to governmental and to private-sector entities in the region. It differs from the traditional approach in what it attempts to accomplish, in its ability to leverage a much larger overall input from nongovernmental sources, and in its likelihood of actually working. This, of course, represents only the potential the process can achieve if it is done right.

As I suggested, the process that begins with the passage of this bill will not respond overnight to the region's economic needs. Indeed, it will not happen at all unless those of us aggressively committed to this program's success combine the forces of the public and private sector to make it work. And if it is to have an input in time to support the kind of Caribbean political leadership that can best benefit from it and best avert a swing back to political extremism in the region, then we have to act now to put in place the practical mechanisms that will bring about this kind of cooperation. The kind of investment that will begin to make the difference must flow substantially from outside the region. This is not to say that Caribbean businessmen and entrepreneurs should not be expected to play a lead role, quite the contrary; few foreign investors will move to commit their resources in countries where local investors fear to tred. But the foreign investor is needed to insure the market access, working capital, managerial expertise and technology to develop whole new major industries quickly. The question is will it be soon enough to provide visible economic and employment gains that local leadership can point to as resulting from U.S. policy.

The Caribbean will benefit from this program to the extent that it results in actual business decisions creating the new markets and new ventures needed to make a visible impact in the regions economies. Large numbers of small and middlesized U.S. firms must be stimulated to set up operations or joint ventures in these countries. U.S. processing and distribution firms need to work out arrangements to purchase dependable quantities of Caribbean products. To reach those hundreds of thousands of American firms which are not aware of the opportunities in the Caribbean, a promotional campaign is urgently needed. This campaign must make U.S. investors aware of the skills, positive business environments, productive capacity, markets and market access potential, local and foreign tax benefits, and other elements that would make Caribbean business options viable and attractive.

My organization has urged the U.S. government to adopt practices on investment promotion that parallel the positive policy implicit in this bill. With government support and collaboration, much of this promotional effort can and should be undertaken primarily by U.S. business leadership, which, after all, best understands how investment decisions are made. Networks need to be established, and diverse sources of potentially relevant information brought together. The U.S. Chamber of Commerce, myriad metropolitan U.S. Chambers of Commerce, investment search arms of U.S. accounting firms, the U.S. Department of Commerce and its field offices—all these and others should be brought into a working relationship in which the U.S. Government and private sector entities can work together to support the desires of Caribbean countries for new and appropriate investment.

AID programs must, in my view, be tailored to enhance the fundamental principles of U.S. policy embodied in this bill. While open access to U.S. markets and a tax credit on investment are positive inducements to the Caribbean and U.S. business communities, they are essentially passive opportunities waiting for something to happen. Notwithstanding these inducements, there remain certain constraints that must be overcome if the desired private sector activity is going to occur. For example, where transportation costs from an island may be prohibitively high, compensating measures might be taken with respect to developing low cost energy potential. In the case of delays at ports caused by inefficiencies or poor facilities, U.S. port and shipping experts could begin working with local officials to identify and solve the problems. Lack of refrigeration facilities are often identified as negatively impacting on shipping of agricultural products. There may be areas where relatively small amounts of focused public assistance could remove the bottlenecks. Publicly assisted trading companies have led the way in the Far East countries to stimulate production for export. U.S. AID is actively exploring some of these possibilities with certain Caribbean Basin countries. These kinds of novel and potentially productive approaches should be encouraged.

Another broad approach which needs attention and encouragement is the strengthening of the private sectors in each of the Caribbean Basin economies. AID and my organization, Caribbean/Central American Action, with help from U.S. chambers of commerce are helping business organizations in the region understand the role they can play to benefit their national economies. Constructive business leadership can play an even more critical role than their governments in taking advantage of the measures in the Caribbean Basin Plan. Energetic business organizations can identify the markets, collaborate with both governments and private sectors to expand production, and generally take the lead in business revitalization.

In summary, you can provide the basic carrot to Caribbean business by endorsing this bill, but passage in itself will not assure the results that only an active business sector can assure. What the administration describes as its "self-help" principle means, in effect, that only the countries themselves can decide how they can best take advantage of these measures. Government can and should set the framework in place, but they cannot do the job. Within this framework, it will be business leadership that will ultimately determine whether the CBI is a success or failure. I have enormous faith in the leadership of business both in the Caribbean and in the United States, if it can be provided with the opportunities for success.

Chairman **GIBBONS**. Thank you, sir.

Our next witness is Mr. Sam Segnar.

Mr. Segnar.

STATEMENT OF SAM SEGNAR, TRUSTEE, CARIBBEAN/CENTRAL AMERICAN ACTION, AND PRESIDENT, INTERNORTH INC., OMAHA, NEBR.

Mr. **Segnar**. Thank you, Mr. Chairman.

My name is Sam Segnar. I am president and chief executive officer of InterNorth, Inc., in Omaha, Nebr. I am testifying today, as it relates to these hearings, because InterNorth has interests throughout the Caribbean in Puerto Rico, the Virgin Islands, the Dominican Republic, Jamaica, Guatemala, Venezuela, and formerly in Haiti.

We have 1,800 employees in this region and all of our employees, supervisors, and officers are natives of the islands or the countries they operate it. It has been my privilege to have been associated with these people as part of an owner company since 1966, and it is those 15 years of activity through the Caribbean Basin that I would like to share with you for a few minutes.

I might add that I also have a statement in writing.

Chairman **Gibbons**. We will put all these statements in the record. Go right ahead.

Mr. **Segnar**. It became evident in the late sixties as I became closely associated with the various countries in the Caribbean Basin that their economies were quite fragile, very dependent on single crops or single exports, and disruptions in the harvest or in the world price of commodities could cause severe hardships within those countries, and the business that it was possible to do was very, very dependent on those fragile circumstances.

As we went into the early seventies and the oil prices escalated rapidly, it appeared to me that these economies started downhill very rapidly. The balance of payments became a severe problem. The GNP became a problem over and over, and unemployment clearly became a severe problem. As unemployment would rise, the area would become unstable, and it was a delicate situation that was being capitalized on by many people.

In the late seventies and early eighties there seemed to be a turn, and with the election of Prime Minister Ciega, there was, in my judgment, an appetite reborn for association with the North. I made it my business to become involved in that, and hence my association as a trustee of the Caribbean/Central American Action.

Now, I think the President's Caribbean Initiative is very, well-founded to move into a situation where there are millions of people crying for help and want to share in American ways and in some of the luxuries that we have available to us.

As a business person, there are some questions that come to mind as we look at free trade, tax incentives, and private investment in that area. I will address these three very briefly.

There is absolutely no question in my mind but what free trade alone will be stimulating and result in the moving of goods and services back and forth between ourselves and the various countries and islands in the Caribbean Basin. Having dealt with trade, that in some cases has not been so free, it is obviously a business constraint that is very difficult to deal with. In particular it is difficult for new arrivals who have not been accustomed to import-export and in dealing with the government agencies and various entities that get involved in the system.

The investment tax credit specifically has already demonstrated that it will enhance investment. All of us, I think, who are in major corporations have taken that advantage, and it will enhance investments. If investment tax credits are made available in the Caribbean, it will also enhance investments there.

Then comes the much more serious question, and I have heard that addressed here this morning: Will we be exporting jobs? Again, all of us who are Americans and all of us in business are very conscious of that question. I think that without a doubt the answer to the question is yes. We will export some jobs; but I would like to remind you—or point out, if I may—that though there is in fact a very large work force to a great extent unemployed in the Caribbean, it is not a source of skilled labor. I cannot imagine that the jobs there would be the skilled jobs that we are upgrading so very rapidly throughout this country.

It is also true that the prevailing wages throughout the area are quite low with the possible exceptions of the Virgin Islands and Puerto Rico. However, that is an opportunity for our own country, and for our own work force, in that it would not be practical to do major manufacturing in any of these islands. But to the extent that we can do subassembly work with low-cost regional labor, and ship the subassemblies back to this country to be assembled by more skilled labor, that makes us more competitive if we can get the job done for less.

I do not think it is using up the type of jobs that we are trying to protect in this country. Yet equally important, to the extent that we can put those people to work at 50 cents an hour or $1 or $1.50 an hour, they become consumers. It is a very interesting experience to take a look throughout this area and recognize that consumers are existing at levels we are not quite accustomed to in this country, and that ranges from quite wealthy consumers down to those who are self-sufficient—meaning they buy nothing; but the instant they have spendable income, they have an instant appetite for goods and services, the majority of which come from this country.

I think in every case in every economy in the Caribbean the balance of trade between ourselves and them is heavily skewed by a factor of 5 to 10 times, with the exception of Venezuela. So I am saying that even though we export a job, we also create a consumer, and that consumer is using a heavy flow of goods from this country, and hence we create jobs in this country.

I have seen and am seeing throughout the area a tremendous attention to the President's initiative. They are looking at us, they are dependent on us, and we have an opportunity to demonstrate to them in the Western Hemisphere, particularly in the Caribbean Basin, that we are working for the mutual good of all of us.

I pray that we will not fail in this effort because if we do, I believe the consequences are unthinkable. So in closing, I endorse the President's initiative as being on the right track. I think that the needs are very significant. The benefits that would flow to ourselves and to the peoples of the Caribbean Basin would be historic.

Thank you very much.

[The prepared statement follows:]

STATEMENT OF SAM F. SEGNAR, PRESIDENT AND CHIEF EXECUTIVE OFFICER, INTERNORTH, INC.

This hearing, I understand, is focusing on those aspects of the Caribbean Basin Initiative package that involve tax and tariff law changes designed to stimulate greater trade and investment in the countries of the Caribbean Basin.

There are three questions, therefore, that we must consider: One—will the intended results happen? Two—if so, will they in fact help the Caribbean economies? And three—if so, will they hurt the U.S. economy?

Briefly, those questions can be answered "one—maybe, two—yes, and three—no." Those short answers obviously reflect some subjective conclusions, based in part upon cold facts and in part upon judgment and experience. What I would like to do today is to elaborate briefly on the reasons I have reached those conclusions.

One—Will the CBI trade and tax measures increase investment in the Caribbean and increase export of Caribbean products into the United States?

This first question is in some respects the most difficult.

The primary incentive tools in the CBI—the Free Trade Area and the investment tax credit—are well designed for their purpose. Their purpose—it is worth pointing out—is to stimulate and benefit Caribbean economies, rather than to confer benefits on potential investors that may be attracted by them. To the potential investor, the effect of having this legislation or not as a factor in global operations or profits is basically neutral; its impact would fall not so much on the basic decision to invest, expand, import, etc., as on the marginal advantage of selecting the Caribbean as an input source or investment site as opposed to somewhere else.

This marginal advantage can be critical for the countries of the Caribbean. But it is important for the U.S. officials implementing the program as well as for potential Caribbean participants to understand that what we are talking about in the CBI package are opportunities, not programs. These opportunities offer great promise, but by themselves their adoption will not change very much. The main reason Caribbean societies aren't exporting more to the U.S. market is not quotas or tariffs. It is the lack of marketing contacts and expertise, transportation problems, and underexploitation of opportunities to develop productive enterprise to meet potential U.S. demand.

This underproduction—or, put another way, lack of sufficient investment—is in turn caused by basic infrastructural deficiences, lack of managerial and technical knowhow, and the simple fact that many potential U.S. investors—whether because of the small scale involved or because of ordinary-garden-variety unawareness—have never really looked at Caribbean potential. It is these factors—not inadequate return-on-investment as such—that are keeping U.S. firms from making more investments in the Caribbean.

The elimination of tariffs and the provision of an investment credit, as proposed in this legislation, will therefore expand the potential for the region's business without in themselves removing the most important obstacles to the immediate expansion or trade and investment.

I point this out not to suggest that these measures are not valuable and important, but merely to underscore the fact that they will not be self-executing, and the further fact that their impact cannot be fully assessed out of the broader context of the untire CBI package, with its additional provisions for economic assistance and private sector institutional development.

Peter Johnson of Caribbean/Central American Action, an organization on whose Board I serve, will be discussing with you in greater detail the type of active Administration strategy we believe will be necessary to mobilize the U.S. business community to recognize and take advantage of these opportunities, and the type of coordinated effort that will be required on the part of U.S. agencies and private sector entities to make the various trade, aid and investment components come together for the right kind of results quickly.

For my part, I wanted to preface my own comments—which will deal primarily with the economic impacts of the trade and investment activity we hope will occur—with the strong observation that these activities will not occur automatically. The U.S. stake in the Caribbean region, coupled with its serious economic problems and the short time fuse we have for addressing them, makes it important that the U.S. Government embarks on this undertaking with a realistic appreciation for the on-going creative and leadership that will be required of it to make this initiative work.

Two—Will the proposed free trade provisions and tax inventives—presuming U.S. and Caribbean companies in fact come forward to take advantage of them—in fact benefit the Caribbean economies?

There are several salient points which I believe need to be raised in connection with both the trade and the tax provisions. In each case, as we look at the potential impact of the expansion over presently existing opportunities, I believe our conclusion will be in the affirmative.

In regard to the Free Trade Area, the basic question is whether—given the present eligibility of so many Caribbean products to enter duty-free under GSP or partially duty-free under Items 806 and 807—the new formula will encompass a large enough scope of additional Caribbean-to-U.S. trade to make a real difference in the Caribbean economies—or enough of a difference to warrant the Reagan Administration's reliance on this Free Trade Area as the "centerpiece" of the CBI.

At least four specific reasons come to mind for viewing the free Trade Area as a significant expansion:

1. While few Caribbean products are presently subject to duty, they are important ones. Rum, for instance, is an industry with significant expansion potential in several of the islands. And exemption from duty on sugar, even within a quota framework, is an important protection for the sugar-growing nations of region—not just the big producers but the small Eastern islands as well. For some of these, staying competitive in the U.S. market represents an enormous concern for them and a negligible concern for U.S. growers, since their total production capacity, though representing 60 percent or more of the local economy, could never supply more than a miniscule fraction of U.S. consumption.
2. While many of the region's products have entered the U.S. market under GSP, the uncertainties of the process have acted as a disincentive to local as well as U.S. investment. In addition to legislatively excluded products, at any given time a wide variety of products can be administratively excluded for long or short periods. Ironically for the beneficiary country, the better its economy does in diversifying into a new GSP-eligible industry, the greater the danger of getting disqualified.
3. The primary purpose of the expanded Free Trade Area concept is not to reduce duties on existing exports from the region, but to encourage Caribbean economies to expand into new industries and new processing phases directed toward U.S. markets they are not presently exploiting. In high-potential areas like electronics assembly, some products now qualify for GSP and others don't. But in either case, Caribbean producers are competing for a small share of a market now overwhelmingly dominated by exporting countries of the Far East. Across-the-board duty-free treatment under the Free Trade Area would give them the marginal advantage they need to develop their natural potential in these fields.
4. In addition to promoting local entrepreneurship and U.S. joint ventures and direct investment, the Free Trade Area concept will support the Administration's basic strategy of spreading the burden for Caribbean development among a broad base of development partners. The liberal value-added provisions—allowing duty-free treatment for any product having even 25 percent of its value added in participating Caribbean Basin countries—will help these countries attract investments and processing business from third countries outside the region.

I might also point out that in addition to these specific benefits, the adoption of the Free Trade Area approach will put the United States in the psychologically responsive posture of opening itself to the most frequently articulated long-term Third World complaint about the international economic system—the lack of access to developed country markets. It makes sense for the U.S. to develop a policy with market access as its centerpiece because the countries to which the policy is primarily addressed have themselves identified that point as central to our relations.

In regard to the proposed tax incentive, as in the case of the free trade provisions, it is important to ask whether the proposed measures will in fact be useful investment attraction tools, recognizing that the primary obstacles to investment lie elsewhere. Again the answer has to be affirmative.

The investment credit against U.S. corporate taxes will put the United States in the position of cooperating with and supporting the many Caribbean countries which have themselves enacted tax holidays and other benefits to attract U.S. investors. Without some corresponding benefit in U.S. tax liability, the pro-enterprise measures of the local governments serve only to transfer the much needed revenues they have foregone to the U.S. Treasury.

A second point is that the U.S. investment credit for the Caribbean Basin cuntries, like the Free Trade Area, will give these countries a marginal advantage in investment attraction against their competitors elsewhere outside the United States.

Third, while the form of the tax credit may not be particularly effective in attracting the type of labor-intensive, low-capital-investment industries many of these countries are courting for quick employment generation, it will serve an important need in attracting the types of industries required in meeting their longer-term development plans. Investment in new plant and equipment will help countries achieve their goals of diversifying out of primary products into more advanced stages of processing, both to cut down on import dependence and to expand the scope of their export marketing.

Finally, investment in new equipment often goes hand in hand with the type of technology transfer and hands-on training that is also critical to the longer term development process.

The third and final major question before us—once we are satisfied that these measures will in fact benefit the Caribbean economies as they are intended to do—is whether they will hurt our own.

I believe we can say with confidence that these measures will not hurt the U.S. economy—and I include in that U.S. business, U.S. labor, the U.S. Treasury, and the U.S. consumer. In fact, I am convinced over the long term we have much to gain.

First, let us look at some of the potential areas of concern, and why they do not in fact represent disadvantages for us.

We are, first of all, dealing in most cases with extremely small quantities. For instance, one of the region's top export products to the United States in 1980 was electronic tubes, transistors and related electronic components, with a total value of $58.6 million. And yet this represented only 1 percent of U.S. imports of this same product category worldwide.

Second, we are not talking for the most part about products to compete with domestically produced products, where new competition would mean harm to U.S. manufacturing firms or loss of American workers' jobs. We are talking about products where the economics of the marketplace has resulted in large scale imports of particular products or product components in any event, where an enormous portion of these imports are derived from a small number of producing countries, largely in the Far East, and where a small shift of some of this production from these countries to those of the Caribbean Basin that are at an earlier stage of development could mean a life-and-death difference for their economic health and future. In many cases, the physical proximity and the opportunities for coproduction involving a Caribbean country and Puerto Rico, or a Caribbean country and a portion of the business being performed in the U.S. mainland, create a situation in which developing the Caribbean industry can actually save U.S. jobs in industries that otherwise could never complete with the 100 percent imported product.

Third, in respect to the investment tax credit, and indirectly to the encouragement of U.S. investment in the Caribbean Basin through the Free Trade arrangement, there may be concern that the result will be decisions by U.S. firms to invest in the Caribbean instead of in the U.S. economy, where the stimulus of new investment is also badly needed. I do not believe such a concern is warranted under the circumstances. The same 10 percent tax credit already applies to U.S. domestic investment. In both cases, the intent is to get businesses that might otherwise be adopting a wait-and-see attitude on interest or inflation, or might otherwise have settled into a comfortable pattern without much new entrepreneurship and risk-taking, to sit up and take a serious new look at putting equity into productive ventures. From my own experience in an industry that has expanded rapidly both domestically and overseas, I do not believe the consideration of new investment options in either category very often takes on an either-or coloration. The market, production and other factors that point to new areas of profitable activity—or, on the downside, make it clear that profitable operations cannot be supported—are complex but highly individualized. The existence or not of the tax credit proposed here would not be a highly salient factor in a company deciding to undertake a foreign venture, and would certainly not be a relevant factor in a decision to forego a domestic one. If, on the other hand, it had decided to expand into foreign operations, or was faced with a situation in which certain aspects of its domestic operations could no longer operate competitively, trade or tax incentives targeted on the Caribbean might be a factor in selecting that region rather than another part of the world as the foreign site. And it might be a factor in the firm deciding to remain an active competitor by dividing its operations in the U.S. and the Caribbean rather than going out of business altogether in the face of foreign competition.

Finally, there is the possible concern about the direct impact on the U.S. Treasury of revenues foregone from the investment tax credit or from the removal of import duties. In the case of duties, I believe it is generally recognized that their primary purpose is not revenue generation but the regulation of the flow of imports and their impact on our economy as a whole. In this instance, the projected $100 to $140 million foregone tariff revenues estimated by our Government not only represents a savings passed along to the consumer—and thus a damper on inflation and a purchasing-power stimulus to the U.S. economy—but also pales in comparison to the real benefit the U.S. economy derives from its trade with the Caribbean Basin. In exchange for the $4 billion worth of Caribbean products the U.S. imports, exclusive of oil, Caribbean Basin countries buy $6.9 billion worth of U.S. exports.

This brings me to a concluding point. In the short term as well as the long term, the U.S. economy and our nation as a whole stands to benefit in a substantial way from our attempt, through the CBI and its various provisions, to boost the economies of the Caribbean region.

In the short term, if we take consistent patterns of past experience as a guide, the surest result of boosting Caribbean exports to the U.S. and to boost even further the levels of U.S. exports to the Caribbean. In the short term also, stimulating U.S. involvement in Caribbean joint ventures and investments can be a way, as earlier mentioned, of keeping U.S. firms competitive and thus saving U.S. jobs while creating new ones in the region.

Over the longer term, the benefits are even more telling.

To our economy, the process of increasing economic development in the Third World—particularly in areas like the Caribbean where social and economic ties with the United States are so tightly woven—can only have a positive impact over time. Higher living standards, more widely diffused, create permanently expanded markets for more and more sophisticated products—the kind our own economy supplies. Hand in hand with this process goes improvements in diet, higher nutritional levels, and ultimately higher demand for the kind of agricultural products which—again—the U.S. is the foremost ultimate supplier. As the world moves into the 21st century, the key to continued expansion and healthy full-capacity production for developed-country economies such as our own will be our ability to nurture and sustain new consumer and industrial markets in the vast areas of the world just now experiencing the possibilities of industrialization.

Another long-term impact we need to keep in mind is the effect of massive immigration from the Caribbean on our own society. It would be foolish and short-sighted on our part to withhold the type of economic assistance and trade concessions now that can turn these societies into healthy, functioning economic systems—knowing that the alternative is a level of desperation, chaos and human suffering that will bring untold thousands to our own shores, where their problems of unemployment and need for human services will then be our own.

Finally, the long-term impact we can never afford to overlook is our own nation's security. The same economic breakdown that will send desperate men and women to our shores would certainly send others, equally driven by desperation rather than by choice, into the arms of our ideological adversaries, and into experiments with extreme political and economic solutions that historically have added to rather than reduced human misery.

An economically battered and weakened Caribbean would be a politically unstable region, prey to violent eruptions and radical realignments. This would represent a danger not only to the $5½ billion worth of U.S. investments there, but more importantly to the security of the United States itself and to the leadership we should be trying to project in our hemisphere and in the world generally.

This frightening scenario need not occur, and is certainly not the choice of the majority of people or governments in the region today. By offering timely assistance now—and I am referring now not only to the trade and tax measures but the entire CBI package including its aid components—the United States can build up healthy local institutions of enterprise and free labor, can nurture attitudes of friendship and respect toward the United States that can only come about as a result of our genuine concern and action for their wellbeing, and can help lay a solid economic foundation for healthy democratic political and social development in the region.

Whatever costs may be involved in carrying out this Caribbean Basin Initiative—and I am convinced they are readily recoverable even in the short term—the cost of doing nothing would be far greater. We are talking about the danger of economic loss, unmanageable immigration, political insecurity, and—somewhere down the road—the danger of the kind of violent upheaval on our shores that could lead to much higher costs. Above all, we are talking about loss of an opportunity—the opportunity to demonstrate not only U.S. compassion toward our immediate neighbors, but the relevance of enterprise and of U.S. economic and political institutions and values to the peoples of the Caribbean and, ultimately, the rest of the developing world.

In a world where our values and our hopes for the future of this planet are so forcefully challenged, and where so many still look to our achievements and our vision with hope for their own future, that is an opportunity we cannot afford to lose.

Chairman **Gibbons**. Thank you, sir.

I noticed, Mr. Johnson, on page 3 of your statement you talk about a conservative trend, and you warn us not to associate it too closely with the so-called conservative trend in this country. Would you explain?

Mr. **Johnson**. The trend I am referring to, Mr. Chairman, is what I referred to in my earlier remarks as well. I am talking about the kind of political leadership that brought into power people like Prime Minister Ciega, Prime Minister Kennedy, Prime Minister Eugene Charles in Dominica, those kind of people who characterize the dynamic Caribbean leadership today, clearly much more moderate, centrist, and certainly conservative compared to what preceded them.

Chairman **Gibbons**. You say our own strategy should not be predicated upon the expectation that the Caribbean governments which are in agreement will stand back and let foreign investors plan their economic future. Would you elaborate on that?

Mr. **Johnson**. Well, the point I am making is that we cannot assume that these governments are going to turn into completely laissez faire type societies. They are going to make some attempt to seek out the kind of investor that will most appropriately deal with the problems that they have. They are going to assert their own rights of sovereignty in this enterprise, but they clearly do want enterprise investment and trade in the United States, but they are going to run it.

Chairman **Gibbons**. Are there other questions for the panel? Mr. Bailey?

Mr. **Bailey**. Thank you, Mr. Chairman.

In this comparison of wage rates, would there be any place in this formula for guaranteeing some kind of transfer to the workers in those countries? If the incentive to invest is, No. 1, a tax incentive that we are going to provide through the use of the investment tax credit or a mechanism very much like it, what is wrong with guaranteeing or seeking some type of guarantee on wages? Is there some problem with that? Is that a bad idea?

Mr. **Segnar**. You are addressing that to me?

Mr. **Bailey**. Yes.

Mr. **Segnar**. I wouldn't characterize the idea as bad, sir, but I would like to comment on the question itself, if I may. While investment tax credit is a help, it is by no means a decisionmaker on whether to invest or not invest.

Mr. **Bailey**. I was going to say that would depend on the situation. As you say, it is a help. You make a decision based upon a group of incentives, and certainly it can be a very important one. I am a great believer in the use of the investment tax credit on directing resource allocation.

I think we need to do what a lot of countries do until they start to do things the way we do in our marketplace, and maybe we can forget about those distortions. Until then, we have to fight smart and fight fairly.

Mr. **Segnar**. Let me address myself, if I may, to a society where the prevailing common labor rate may be 50 cents an hour. Admittedly and for sure, the living standards are quite low compared to our own; however, they are the standards that the country at this moment in time is accustomed to, and with, let me say, a 20- or 40-percent unemployment rate, having an opportunity for a job at 50 cents an hour, as modest as that sounds to us, is a tremendous incentive in that locality.

Now, as soon as we start by raising that rate, it occurs to me that there will be fewer jobs and that the name of the game is jobs, and when that unemployed pool is used up, you can be sure the 50 cents will turn into 60 and will turn into 70.

Mr. **Bailey**. Is there any validity to the argument made that that labor in those countries is being used? I mean if we are going to transfer the benefits of a free enterprise, capitalistic system, let's transfer them to everybody, at least in some degree. I don't have a figure for you. I really don't know. We talk about the transfer of value added from what is done in the Far East, investment attraction, from what is done in the Far East to the Caribbean, and we are talking about creating some kind of demand for U.S. products down there and that kind of thing.

I think some of these ideas we are talking about are OK, but I also think this country has just got to get its feet on the ground with some kind of coordinated policy, and we don't have it yet. It also makes the American taxpayer comfortable with what we are doing.

You see, it is easy for us to sit here and talk about the displacement of jobs, but I happen to live in an area where population is declining, labor is leaving, people are leaving. It is devastating. It is easier for us to sit here and talk about a factory that closes down, you see, and then have at the same time a government whose policy it is to eliminate those programs that give those nameless, faceless, unemployed people whose lives have been altered—and forgive my emotion—perhaps for the rest of their lives, in some cases, no kind of really decent assistance on training them to move into this beautiful, high technology world into which we are moving and which we are exporting to the Japanese via other mechanisms.

I know you are very well intentioned, and I think you are right on target with the things that we need to do. I just don't know how much we make America attractive and free enterprise attractive unless we look at these situations from an overall point of view. Now, you want to go in and give them a 50-cent-an-hour job. You are going to attract a lot of investment to do that, but you are not going to take the mechanisms there to allow those people to progress and move up and get a little more of the income that is being transferred.

You establish a certain industry there. That money comes back, the products are sold here. What is done with the proceeds of the profits made in this country on those increased sales? Some of it goes to our Treasury and our distribution system. We get some benefits from it. There is some spin-off, I realize that.

Mr. **Segnar**. I appreciate your emotion, sir, and share at least some of it. The distribution of profits through the corporate system obviously goes to shareholders in the course of time.

I would like to say one more thing. Again, we have coined the phrase, 50-cent-an-hour job. In that particular society that is a very, very important job. And I very much appreciate your concern about our exporting our American way, and through the countries that I am in business that I have described and where there is a range of base pay, I can just assure you when those involved, whether it be at 50 cents an hour or $5 an hour, are in the system, the incentive system, work for compensation and have their own spendable income, modest as it may be or significant as it may be, they begin to participate in our system.

Mr. **Bailey**. OK. I know what you want to accomplish down there, and maybe we get up here and our income gets a little high or something and maybe we forget where we came from. I have not been here that long. I do not forget where I came from. I do not forget working on a job that did not have medical benefits, and I can still remember cleaning chicken coops and all that good stuff.

Mr. **Segnar**. I share that, sir.

Mr. **Bailey**. How about something going hand in hand, then, with initiatives of this sort to do something about American employment and jobs? Now, we have some ideas. We just sat down at the subcommittee. Our chairman is very fair, trying to work with us, trying to do something about it, especially us folks from areas that are really affected.

We have a fight on our hands to just provide training money for people who are going to lose a job once the industry is gone. You know, what happens to a family up there when their home goes and they have got that 30-year mortgage? Try to sell a house today. When the job goes the bank does not even want to foreclose. It is the only advantage they have. They have kids in school, too.

We have a standard of living we built and created here that we have a right to look at. And I want to help those people down there. I know what people like that can live through and go through. But I think you have to do something about the entire economic system in all its ramifications.

Let me end with one last statement. Alternative minimum tax, are you familiar with that?

Mr. **Segnar**. Yes, sir.

Mr. **Bailey**. All right. What is your view on that? Is that consistent with the Caribbean Basin Initiative philosophically? Is it consistent as a matter of tax policy?

Mr. **Segnar**. I do not——

Mr. **Bailey**. You do not see any connection at all?

Mr. **Segnar** [continuing]. View the tax policy as necessarily a matter of consistency throughout.

Mr. **Bailey**. You do not see any connection or philosophically you do not have any difficulty with the proposal of alternative minimum tax and the philosophy being discussed in this Caribbean Basin Initiative at all? I mean, I am supposed to say to an American businessman that we want to pass this alternative minimum corporate tax, and then I am going to go out on the other hand and vote a Caribbean Basin Initiative?

You see, interdependent trade to business people who operate in the international sense has got to have some aspect of fairness to it. You do not see any connection at all there?

Mr. **Segnar**. Yes, sir, I see what you are talking about, and I in fact agree with what you are saying. However, in fact when I start examining tax laws and tax procedures, I do not find consistency and equity at all across the entire course of tax laws.

Mr. **Bailey**. We might mean it in a different way. But I see Guy Vander Jagt over here chomping at the bit. All right. I thank you for the chance to get a couple things off my chest.

Mr. **Segnar**. I thank you for doing so. I appreciate your raising the question of our taking jobs in effect to the Caribbean Basin when we are indeed having severe hardships in a number of areas in our own country and possibly even all over. And I have thought about that more than you might believe, and I do not have an answer for it, nor do any of us have an answer for it.

But here is where I have come out. We will work our way through the unemployment, the 9 percent or even if it is more, and we will, with due hardship admittedly, get our people relocated, retrained, and back on jobs and back in their houses. In the meantime we have what I consider to be a window of some relatively short duration in this Caribbean area, and if we do not somehow get help to those people somebody else will.

And if that happens, I think that we will be in a circumstance much worse than even the matter of our 9 percent unemployment in this country right now. What I am saying is, we have to do both.

Mr. **Bailey**. Senator——

Mr. **Segnar**. Sir, I am not a senator. I am Sam Segnar.

Mr. **Bailey**. I apologize.

Mr. **Segnar**. I enjoyed the title. [Laughter.]

Mr. **Bailey**. I apologize. I am sorry.

Let me say this to you. I share those goals and I understand them very well. I am very familiar with what went on in Jamaica. I know what this country, for example, does not seem capable of doing with its intelligence community that other countries have. You may be more familiar with more details. I am.

There are a lot of things we could do and it is very hard for me to separate out without sounding like a myopic individual who is just trying to demagog on an issue. But I have a sincere concern for doing something with these policies and doing it in a meaningful way.

I just have sincere doubts on whether the way you are doing this really makes that much sense in terms of the kind of help that we need to provide down there. Economic incentives, yes. I think some of the vehicles being suggested here just do not make the best sense, and they are very difficult to sell to the American people. We need American confidence in foreign aid. We do not have American confidence in foreign aid, and I do not think this is going to help much. That is my fear.

So I thank you, Mr. Chairman.

Chairman **Gibbons**. Thank you very much.

Mr. **Segnar**. Thank you, sir.

Chairman **Gibbons**. We next have a rather large panel for the Coalition of Leather Products Industries. I wish the panel would come forward. And while the panel is coming forward we will put some signs down there.

Mr. Nehmer, you are the first here, you are in the middle and you have got the mike. So you proceed, and then we will just go as you would like at the table.

STATEMENT OF STANLEY NEHMER, PRESIDENT, ECONOMIC CONSULTING SERVICES, INC.

Mr. NEHMER. Thank you very much, Mr. Chairman.

For the record, my name is Stanley Nehmer. I am here with a group of representatives of trade associations and labor unions in the leather products industry, and the organizations we represent are listed in my testimony and in the individual pieces of testimony.

Chairman GIBBONS. And as you know, all of this will be included in the record just as you have presented it here in these written statements.

Mr. NEHMER. Thank you very much, Mr. Chairman.

Not all of us listed in the witness list will be making statements. Those of us who will be will be summarizing our remarks so that we will meet the time constraints that have been suggested to us.

Chairman GIBBONS. Thank you.

Mr. NEHMER. The administration's Caribbean Initiative has the goal of promoting the economic well being of the people of the Caribbean area and of alleviating the economic crisis that threatens them. The organizations before you at this time certainly support this goal and the aspirations of the Caribbean peoples.

However, those who work in leather-related industries in the United States have similar aspirations for themselves and their families, and they are also facing serious economic problems arising out of growing volumes of imports. They see in the duty-free proposal of the Caribbean Basin Initiative a further export of their jobs to Carribean countries which are already substantial suppliers of competing leather products and have the ability, with their large pool of cheap labor, to increase their exports to us even further.

Given the vulnerability of this industry to imports, we seek an exclusion from the free trade provisions of the CBI as has already been decided for textiles and apparel.

I would like to summarize and then we will hear from individual members of the panel.

First, imports of leather-related products from the potential beneficiary countries in the Caribbean are already substantial and they are growing.

Second, imports of leather products into the United States already enjoy, if I may use that word, a very large share of the U.S. market. In the case of shoes, leather wearing apparel, and leather work gloves, imports account for 50 percent, in that order of magnitude, of our market. Handbag imports account for at least 75 percent of the U.S. market. Luggage imports have 36 percent of the U.S. market. Personal leather goods imports have 25 percent of the U.S. market.

Third, increased imports from the Caribbean under one-way free trade will not replace imports from other countries, but rather will be at the expense of U.S. firms and their workers. We have found over the years that many developing country producers have entered the U.S. leather products market with few displacements, if any, of older developing country suppliers.

We have a case in point of one leather product that did receive zero-duty treatment under the generalized system of preferences when it began in 1976, and 3 years later it was removed from the preference list. This is leather wearing apparel. The statistics show very dramatically how zero-duty treatment of leather wearing apparel resulted in very large increases in imports.

Imports from Korea in the year before GSP treatment was accorded were $25 million. In the first year of GSP it was $66 million, going up to $79 million, then going up to $114 million by the third year. Argentina shipped us $3 million worth of leather wearing apparel before GSP. In the first year of GSP it was $10 million. In the second duty-free year it was $18 million. In the third zero-duty year it was $44 million.

Fourth, the U.S. leather-related industries are labor intensive and employ about a quarter of a million workers. They are mostly semiskilled. The work force generally consists of women and minorities. In addition, these industries generally provide entry-level jobs for people under 25 or over 50, the age groups which are the hardest to employ and which have the highest unemployment rates.

In two pamphlets published by the group that preceded us, the Caribbean Central American Action, information is presented on what the wage rates are in Dominica and St. Lucia. In Dominica, the semiskilled workers wage rates in U.S. dollars are 65 cents to a dollar an hour. The skilled technicians receive $1.25 to $2 an hour. In St. Lucia, assuming a 40-hour week—and I am not clear what the workweek is, but on the basis of a 40-hour week—the unskilled workers in manufacturing receive 55 cents an hour; the semiskilled workers receive $1.63 an hour.

These are the same types of workers, the same kinds of skills that appear in the leather products industry in the United States.

Fifth, virtually all firms in these industries in the United States are small businesses, that is employing 500 workers or fewer. Only 5 days after President Reagan submitted his Caribbean Basin Initiative plan to Congress, he also had a big ceremony with regard to the importance of preserving small business in the United States. He pointed out that small business is the heart and soul of our free enterprise system and that over half of our labor force is employed by small businesses, that most small firms are labor intensive, that small business provides most by far of the new jobs in the economy. And finally, America needs small business formation or growth.

The administration cannot simultaneously permit duty-free entry of leather products from the Caribbean and foster these small businesses. We do not believe these small firms and their workers should be considered an expendable contribution for national policy objectives, as important as they may be.

Sixth, these products we are talking about today have already been determined to be import-sensitive, either specifically in legislation passed by Congress or in actions taken by the executive branch.

Seventh, a very important trade policy change is being made through the proposal for duty-free treatment. The policy that is being proposed flies in the face of all trade legislation in recent years. And we should make no mistake about it: the duty-free provisions of the Caribbean Basin Initiative represent a dramatic change in U.S. trade policy, and as it applies to leather products it is a harmful change. Why? Because it is discarding the concept of import sensitivity.

Eighth, we are assured that there are safeguard provisions that will protect U.S. firms and workers from injury because of duty-free treatment. Actually, the safeguard provision that is proposed in the existing legislation that has been sent to the Hill by the administration has been tried over the years and has been found not to work is the escape clause. Only 9 petitions out of 45 since the Trade Act of 1974 went into effect have resulted in import relief.

Nonrubber footwear was the subject of a discontinuation of import relief by President Reagan on June 30, 1981, which does not give this group of industries very much comfort as to the future.

We feel our industry is already in a state of siege. We have suffered from plant closings and lost jobs due to imports, and we look to Congress for help in preventing further damage. We ask that leather products be excluded from the one-way free trade provisions of the Caribbean Basin Initiative.

[The prepared statement follows:]

STATEMENT OF STANLEY NEHMER, PRESIDENT, ECONOMIC CONSULTING SERVICES, INC.

My name is Stanley Nehmer. I am President of Economic Consulting Services Inc. We are consultants to several trade associations and labor unions in the leather products industry. I am here with representatives of these organizations whose members will be directly affected by the trade measures proposed as part of the Administration's Caribbean Basin Initiative. These organizations are:

Amalgamated Clothing and Textile Workers Union, AFL-CIO Footwear Industries of America, Inc.; International Leather Goods, Plastics, and Novelty Workers' Union, AFL-CIO; Luggage and Leather Goods Manufacturers of America, Inc.; National Handbag Association; Work Glove Manufacturers Association; and United Food and Commercial Workers Union, AFL-CIO.

The Administration's Caribbean Basin Initiative has the goal of promoting the economic well being of the people of the Caribbean area and of alleviating the economic crisis that threatens them. The organizations before you at this time certainly support this goal and the aspirations of the Caribbean peoples. However, those who work in leather-related industries in the United States have similar aspirations for themselves and their families, and they are also facing serious economic problems arising out of growing volumes of imports. The Caribbean countries are already substantial suppliers of competing leather products and have the ability with their large pool of cheap labor to increase their exports to us even further.

It is manifestly unfair to have firms and workers in the leather products industry pay for this national policy initiative. Given the vulnerability of this industry to imports, we seek an exclusion from the free trade provisions of the Caribbean Basin Initiative as has already been decided for textiles and apparel, which are similarly labor-intensive and import-impacted industries.

The leather goods industry should receive this exclusion for a number of important reasons.

First, imports of leather-related products from the potential beneficiary countries in the Caribbean are already substantial and growing. Imports of handbags, for example, were valued at $14 million in 1981, up 8 percent from the previous year. Non-rubber footwear imports from these Caribbean countries in 1981 were $10.4 million, at increase of 59 percent over the previous year.

Second, not only are leather product imports from the Caribbean sizeable and growing, but they are also increasing their penetration of the U.S. market together with imports from other countries. Imported handbags from all sources, for example, accounted for 29 percent of the U.S. market in 1967 but held over 75 percent in 1981. Over the same period, imports of non-rubber footwear have increased their share from 18 percent to 50 percent. The trend is the same for other products such as leather apparel, luggage, leather work gloves, and personal leather goods. The key point is that Caribbean exporters do not need duty-free entry in order to penetrate and compete in the U.S. market.

Third, increased imports from the Caribbean under one-way free trade will not replace imports from other countries but rather will be at the expense of U.S. firms and their workers. Over the years, many developing-country producers have entered the U.S. leather products market with few displacements, if any, of older developing-country suppliers.

Fourth, the U.S. leather-related industries are labor intensive and employ about 250,000 workers. They are mostly semi-skilled and generally women and with minorities marking up a large portion of the work force. Indeed, a large portion of these workers came to the United States from the Caribbean, some quite recently. In addition, these industries generally provide entry-level jobs for people under 25 or over 50, the age groups which are the hardest to employ and which have the highest unemployment rates. The loss of jobs for these people would be tragic, even more so in light of both the reduction in Federal funds for Trade Adjustment Assistance and the reduced ability of state governments to offer assistance as they take on additional burdens.

Fifth, as virtually all firms in these industries are small businesses, the closing of such companies would be tragic, coming as it would when the President has pledged himself to a program to promote small business. In his March 1 report to Congress on small business, the President said that "small business is the heart and soul of our free enterprise system." He further pointed out that over half of our labor force is employed by small businesses; that most small firms are labor intensive; that small businesses provide most, by far, of the new jobs in the economy; and that "America needs small business formation or growth." Yet, the one-way free trade provisions of the Caribbean Basin Initiative will result in increased imports to the serious deteriment of firms and workers in the leather products industries. The Administration cannot simultaneously permit duty-free entry of leather products from the Caribbean and foster these small businesses. We do not believe that these small firms and their workers should be considered an expendable contribution for national policy objectives, as important as they be.

Sixth, the Congress and the Executive Branch have already recognized the import-sensitivity of the leather-related industries. Nonrubber footwear was specifically excluded from the Generalized System of Preferences (GSP) in the Trade Act of 1974. Virtually all leather-related products have been found to be import sensitive in the context of GSP. The International Trade Commission (ITC) found that imports were a substantial cause of the injury suffered by the leather apparel and nonrubber footwear industries. Furthermore, four of the leather-related industries represented here today—footwear, luggage, work gloves, and handbags—have all received EDA grants to improve their competitiveness vis-a-vis imports, specifically because they were import impacted. How can the Executive Branch recognize the import sensitivity of these leather-related industries and yet propose duty-free legislation that will only worsen the health of these industries?

Seventh, we understand that 87 percent of our imports from the Caribbean enter duty free under the GSP program. By following the remaining 13 percent of imports (with the exception of textiles and apparel) to enter duty free as well, we fear that the Administration is discarding the concept of import-sensitivity and is moving to zero duty for those items which are import sensitive. Such a policy flies in the face of all trade legislation in recent years. There should be no mistakes about it: the duty-free provisions of the Caribbean Basin initiative represent a dramatic change in U.S. trade policy. Unfortunately, as it applies to leather products it is a harmful change.

Eighth, the Administration assures us that existing safeguard measures will be adequate to protect U.S. firms and workers from injury due to increased imports generated by one-way free trade. The existing safeguard measures, however, do not work for the leather products sector. It is characteristic of these industries that imports can increase rapidly before safeguard action can be taken, regardless of how good the intentions of the Executive Branch may be. Certainly the record of the "escape clause" in the United States leaves serious doubt as to how effective a safeguard would be under the CBI. Out of the 45 investigations completed to date under Section 201 of the Trade Act of 1974, only 9 have resulted in import relief. Action taken by the President on June 30, 1981 to terminate relief on nonrubber footwear is a clear indication of what may lie ahead for the leather-related industries. Furthermore, the Administration's trade policy statement of July 8, 1981 suggests that industries such as ours should be concerned about the effectiveness with which the Administration will apply safeguards in the future.

In conclusion, with substantial and growing import penetration, the leather-related industries are already in a state of seige. They have suffered from plant closings and lost jobs due to imports. These industries look to Congress for its help in preventing further damage. We ask that leather products be excluded from these one-way free trade measures. Do not exacerbate our problems in the name of a national policy initiative. Do not cause more of our plants to close. Do not make our workers pay for this new policy.

STATEMENT OF ART GUNDERSHEIM, DIRECTOR, INTERNATIONAL TRADE AFFAIRS, AMALGAMATED CLOTHING AND TEXTILE WORKERS UNION, AFL-CIO

Mr. GUNDERSHEIM. I am Art Gundersheim, assistant to the president and director of international trade affairs for the Amalgamated Clothing and Textile Workers Union. And I thought for a quick instant maybe I should have let the prior witness make my case for me, since he talked about the positive transfer of jobs, but I think it needs a little embellishment.

I certainly would have to say at the outset that we support the President's initiative with regard to the Caribbean. It is important that its objectives are realized. We recognize that the Caribbean area is one where political, economic, and social stability are so important to the security and economic well-being of our own country. If this policy is successful, it will help the free trade union movement in that area, which in itself will contribute mightily to the democratic process.

Having said that the new trade arrangements with the Caribbean cannot result in the closing of U.S. plants, American workers cannot be made to pay for this initiative. No individual sector or group of sectors in our economy should bear an inequitable portion of the burden.

It is for these reasons that we believe that shoes, leather wearing apparel and other leather-related products should receive similar treatment that has been recognized in terms of textiles and apparel and that is to be excluded from duty-free entry.

Import sensitivity and import injury sustained by nonrubber footwear has certainly been well-documented. Nonrubber footwear was specifically excluded by Congress from the GSP system in the Trade Act of 1974. Leather apparel was removed from the GSP list in 1978, as I recall.

The ITC has found in numerous instances, some cited by Mr. Nehmer, and additional instances in every case that has come before the ITC dealing with nonrubber footwear or leather apparel, the ITC has found that both of these industries have sustained substantial import injury and have recommended relief of one type or another.

It has been our unfortunate experience that in some of these instances, particularly in the last couple of years, relief was not forthcoming. Both under President Reagan and under President Carter, after unanimous findings of injury, the import relief recommended or a substitute was not granted by the President. In fact, therefore, our people have no faith in the import relief mechanisms set forth in the Caribbean Basin Initiative and those others provided by law in the Trade Act.

We cannot rely upon these avenues to seek relief when imports from the Caribbean would increase very substantially because of the duty-free treatment. In fact, for the footwear industry the escape clause provisions are not available to us until more than a year from now because of the requirement that we cannot reapply for injury relief before 2 years after the expiration of the prior import relief.

As has been enumerated to you, both the nonrubber footwear industry and the leather apparel industry are suffering from penetration somewhere around the 50-percent level in the U.S. market. We can translate these into jobs and can do so in terms of the statements that you have. There are thousands upon thousands of jobs that are already lost due to these imports, and here is a policy deliberately set up to increase that job loss.

On the other hand, this country has a specific need for and, indeed, an obligation to provide entry-level or lower skilled jobs to certain segments of the population who for a large number of reasons cannot readily find alternative employment. An economic base which supplies entry-level of low-skilled jobs to those segments of the population which cannot otherwise be employed is critically important for the long-term economic stability in the United States.

So long as our country remains a beacon for the dispossessed in the rest of the world and so long as we must rely on the private sector for job creation in our society, we absolutely need to preserve industries such as the footwear industry and leather apparel industry to give employment to large, large numbers of people who have no other place to go.

We believe that the workers in the leather-related industries will be among the sectors hardest hit by one-way free trade proposal, obviously because of the labor intensity of this industry, obviously because of the already well-established import markets that have been developed by several of the countries.

It is for these reasons that we believe very strongly that shoes, leather apparel, and other leather-related products should be excluded from duty-free treatment under the Caribbean Basin Initiative, and we urge the subcommittee to amend the current legislation to incorporate this when it reports the bill out.

Thank you very much.

[The prepared statement follows:]

STATEMENT OF AMALGAMATED CLOTHING AND TEXTILE WORKERS UNION, AFL-CIO AS PRESENTED BY ARTHUR GUNDERSHEIM, DIRECTOR, INTERNATIONAL TRADE AFFAIRS

Members of the Subcommittee, my name is Art Gundersheim, Director of International Trade Affairs for the Amalgamated Clothing and Textile Workers Union, AFL-CIO. In addition to representing workers in the textile and apparel industries, our Union of some 500,000 members also represents workers producing shoes and leather apparel.

We recognize the Caribbean area as one where political, economic, and social stability are so important to the security and the economic well-being of our own country. If the Caribbean policy is successful, it will help the free trade union movement in that area, which in itself will contribute mightily to the democratic process.

We support the President's initiative with regard to the Caribbean. It is important that its objectives are realized. But having said this I must make it clear that organized labor has concerns on its implementation which must be met if the new policy is not to cause hardship to firms and workers in this country. Here I refer specifically to the one-way free trade aspects of the Caribbean Basin initiative.

In the November 1981 Convention of the AFL-CIO the resolution on trade and investment included the statement:

New proposals for trade arrangements with America's nearest neighbors, or with any other individual foreign country, should be based on a realistic assessment of the past and future impact of trade and investment not only in the host country but on specific parts of the U.S. economy and on U.S. workers.

What this means is that labor wants to help in this new initiative but it cannot be done at a price that we cannot bear. The new trade arrangement with the Caribbean cannot result in the closing of U.S. plants. American workers cannot be made to pay for this new initiative. No individual sector or group of sectors in our economy should bear an inequitable portion of the burden.

For these reasons, we believe that shoes, leather apparel, and other leather-related products should receive similar treatment to that being accorded textiles and apparel under the CBI and should be excluded from duty-free treatment.

The import-sensitivity and import injury sustained by both the nonrubber footwear and the leather apparel industries are well documented. Nonrubber footwear was specifically excluded from the Generalized System of Preferences by the Trade Act of 1974. Leather apparel was removed from the list of eligible articles under the GSP because of its import sensitivity. The U.S. International Trade Commission found that imports were a substantial cause of the injury suffered by both the nonrubber footwear and leather apparel industries. However, at the present time there is no import relief in effect for either of these industries. Leather apparel did not receive relief, despite a unanimous finding of injury by ITC in 1980. Similarly shoes were unanimously found by the ITC to continue to need import relief just last year. Once more workers and firms were rebuffed when the President terminated import relief on nonrubber footwear as of June 30, 1981. Thus our people have no faith in the import relief mechanisms set forth in the Caribbean Basin Initiative. We cannot rely upon these avenues to seek relief when imports from the Caribbean increase because of duty-free treatment. Indeed, there is no option open to the footwear industry under the "escape clause" until July 1, 1983, 2 years after the expiration of import relief.

Both the nonrubber footwear industry and the leather apparel industry are suffering from import penetration hovering at the 50 percent level. Thousands of jobs have been eliminated in these industries as a result of increasing imports.

With respect to leather apparel, U.S. imports achieved tremendous growth during the latter part of the 1970's, rising from $131 million in 1975 to $318 million in 1978. After declining somewhat since 1978, concurrent with reduced domestic demand for these products, imports jumped more than 20 percent in 1981 compared to levels of 1980. We estimate that approximately one-half of the firms in the leather wearing apparel business in 1975 are no longer in business today or are no longer producing leather apparel, and that domestic production has declined by approximately 50 percent since that time. Both employment and average hours worked in this industry have also declined markedly.

With respect to footwear, our industry remains in serious trouble because of the unsolved import problems. Today, there are approximately 20,000 fewer production workers in this industry than in 1976. Imports increased again in 1981 after a temporary decline in 1980, and increased particularly in the last half of 1981 after import relief was terminated. Production is at a post-war low. Employment continues to decline.

Duty-free treatment for all imports other than textiles and apparel from the Caribbean has the potential for seriously affecting the footwear, leather apparel and other leather-related industries. We are particularly concerned about a further loss of job opportunities for our workers. This country has a specific need for, and indeed an obligation to provide, entry-level or lower-skilled jobs to certain segments of the population who, for a variety of reasons, cannot readily find alternative employment. An economic base which supplies entry-level or low-skilled jobs to those segments of the population which cannot otherwise be employed is critically important for the United States. Unemployment and all its serious attendant social problems cannot be accepted as the norm for these workers. So long as our country remains a beacon for the dispossessed of the rest of the world and so long as we must rely on the private sector for job creation in our society, we absolutely need to preserve industries such as those in the leather products sector.

There is no one to bear the burden of increased domestic unemployment created by the CBI but the workers themselves. There are likely to be no trade adjustment assistance benefits to help them along. Even welfare benefits are being cut back. We believe that workers in the leather-related industries will be among the sectors hardest hit by the one-way free trade proposal, primarily because of the labor-intensity and import-sensitivity of these industries.

Shoes, leather apparel and other leather-related products should be excluded from duty-free treatment under the CBI. I urge the Subcommittee to amend the current legislation to incorporate our products similar to the exclusion granted textiles and apparel.

Thank you.

Mr. NEHMER. Mr. Marvin Hrubes for Mr. Wynn.

STATEMENT OF MARVIN R. HRUBES, EXECUTIVE ASSISTANT TO THE DIRECTOR OF PUBLIC AFFAIRS AND COMMUNICATIONS DEPARTMENT, UNITED FOOD AND COMMERCIAL WORKERS INTERNATIONAL UNION, AFL-CIO, ON BEHALF OF WILLIAM H. WYNN, PRESIDENT

Mr. HRUBES. Mr. Chairman and members of the subcommittee, my international president, Bill Wynn, asked me to apologize for his being unable to attend due to scheduling, but he has asked me to read some of the highlights of his testimony into the record.

United Food and Commercial Workers is a labor union with 1.3 million workers organized in some 700 local units throughout the United States and Canada. The local unions have collective bargaining agreements with tens of thousands of employees throughout the food processing, retail sales, leather, health, commercial, shoe, fur, and other industries.

I am here today on behalf of our shoe workers and as part of a group of industry and labor representatives in the leather products sector who show a strong concern over the one-way free trade aspects of the Caribbean Basin Initiative.

It is clear to us that certain segments of the U.S. population and work force should not be made to pay for the Caribbean Basin Initiative. We believe that duty-free treatment for all products other than textiles and apparel imports from the Caribbean will have a negative impact on firms and workers in the leather products sector.

We believe that leather-related products should be excluded from duty-free treatment under the CBI because of their import sensitivity and the import injury already sustained by these industries. The bill before the subcommittee should be amended to cover leather-related products in the exclusion from duty-free treatment as is being accorded textiles and apparel.

What is at stake here is jobs. With 9 million workers unemployed in the United States, it is inconceivable that we should initiate a policy which could result in further job losses. The shoe industry provides employment for more than 140,000 workers, although thousands of shoe workers have lost their jobs over the past several years.

A major cause for the reduced work force has been imports, which have increased and relentlessly captured an inordinately large share of the U.S. footwear market. Today one out of every two pair of shoes sold in this country is imported.

Clearly, the primary means by which imports of shoes and most other leather-related captured a substantial mark share is price. The highly labor-intensive production process results in labor costs which represent a major portion of total production cost.

While U.S. workers in the leather products sector earn an average of less than $5 per hour, workers in the Caribbean are paid something on the order of 50 cents to $2 per hour. Wages in the U.S. leather products sector are substantially below the average wage for U.S. industrial workers, yet they are undercut by still lower foreign wages.

As a result, imports from low-wage developing countries such as those in the Caribbean already have a substantial price advantage over U.S.-made products. These countries do not need duty-free treatment to penetrate the U.S. market for shoes in a substantial way.

In addition to jobs, all of the industries in the leather products sector are concerned with safeguards. Those of us worried about the viability of the footwear industry have a particularly strong reason to be concerned. Under the escape clause provisions of the Trade Act of 1974, there can be no investigation with respect to products which were the subject of import relief unless 2 years have elapsed.

President Reagan terminated relief for the nonrubber footwear industry as of June 30, 1981. Thus, the nonrubber footwear industry cannot seek import relief again until July 1, 1983. The safeguards in the proposed legislation do not change this. A lot can happen in the interim, and we have absolutely no avenue of relief open to us and no way to redress injury caused by increased imports from the Caribbean.

In this industry in particular, we have watched as imports from developing countries increased rapidly. Imports of shoes from Hong Kong are a case in point, and even more recently, imports from the People's Republic of China. We have no reason to believe that Haiti or the Dominican Republic or any of the other Caribbean Basin countries will not be the next developing country to enter the U.S. market in a bigger way.

Imports of nonrubber footwear from Haiti jumped from 774,000 pairs in 1980 to 1.2 million pairs in 1981, an increase of 55 percent in just 1 year. The reasons for our concern should be eminently clear. Workers in the shoe industry and the other leather-related industries must be spared from any further import injury which is likely to result if imports from the Caribbean receive duty-free treatment. Shoes and leather-related products must be excluded from the free trade provisions of the CBI.

Thank you.

[The prepared statement statement follows:]

STATEMENT OF WILLIAM H. WYNN, PRESIDENT, UNITED FOOD AND COMMERCIAL WORKERS UNION, AFL-CIO

My name is William Wynn, President of the United Food and Commerical Workers Union, AFL-CIO. The UFCW is a labor union with 1.3 million workers organized in some 700 local unions throughout the United States and Canada. The UFCW and its local unions have collective bargaining agreements with tens of thousands of employers throughout the food processing, retail sales, leather, health, commercial, shoe, fur and other industries. I am here today on behalf of our shoe workers and as part of a group of industry and labor representatives in the leather products sector who share a strong concern over the one-way free-trade aspects of the Caribbean Basin Initiative.

At the outset, let me say that we support the AFL-CIO position that "aid in the development of Caribbean nations needs to be enhanced, but proposals for 'one-way' free trade and additional investment incentives to U.S. firms for investing abroad should be rejected." It is clear to us that certain segments of the U.S. population and work force should not be made to pay for the Caribbean Basin Initiative. We believe that duty-free treatment for all products other than textiles and apparel imports from the Caribbean will have a negative impact on firms and workers in the leather products sector. We believe that leather-related products should be excluded from duty-free treatment under the CBI because of their import-sensitivity and the import injury already sustained by these industries. The bill before this Subcommittee should be amended to cover leather-related products in the exclusion from duty-free treatment as is being accorded textiles and apparel.

What is at stake here is jobs. With 9 million workers unemployed in the U.S., it is inconceivable that we should initiate a policy which could result in further job losses. The shoe industry provides employment for more than 140,000 workers, although thousands of shoe workers have lost their jobs over the past several years. A major cause for the reduced work force has been imports, which have increased and relentlessly captured an inordinately large share of the U.S. footwear market. Today, one out of every two pairs of shoes sold in this country is imported.

Clearly, the primary means by which imports of shoes and most other leather-related products have captured substantial market share is price. The highly labor-intensive production process results in labor costs which represent a major portion of total production costs. While U.S. workers in the leather products sector are earning an average of less than $5.00 per hour, workers in the Caribbean are paid something on the order of $.50 to $2.00 per hour. Wages in the U.S. leather product sector are substantially below the average wage for U.S. industrial workers, yet they are undercut by still lower foreign wages. As a result, imports from low-wage developing countries such as those in the Caribbean already have a substantial price advantage over U.S.-made products. These countries do not need duty-free treatment to penetrate the U.S. market for shoes in a substantial way. In fact, it is important to recognize that shoes were excluded from duty-free treatment under the Generalized System of Preferences precisely because of their import-sensitivity. Is the Administration implying that the potential for injury from imports from the Caribbean is any less than from other designated beneficiary developing countries under the GSP? By allowing shoes and other leather products to enter duty-free under the CBI, is this country now abandoning all concepts of import-sensitivity and moving toward zero duty for products which *are* import-sensitive? This is clearly not an acceptable position from our standpoint. Nor do we think that this is a publicly supportable policy.

One of the reasons we are particularly concerned about the CBI and its effect on import-sensitive industries such as ours is the lack of an effective safeguard mechanism to adequately protect domestic industries from import relief. Only 9 investigations completed under the "escape clause" provisions of the Trade Act of 1974 resulted in import relief. Footwear was one of those industries. You may be aware, however, that Congress through the Senate Finance Committee had to intervene and initiate an "escape clause" proceeding for this industry in 1976, after the industry had proven serious injury and yet received no import relief from President Ford. On the second try, import relief was granted by President Carter; however, President Reagan terminated relief for the nonrubber footwear industry as of June 30, 1981.

All of the industries in the leather products sector are concerned with regard to safeguards. Those of us concerned with the viability of the footwear industry have a particularly strong reason to be concerned. Under the "escape clause" provisions of the Trade Act of 1974, there can be no investigation with respect to products which were the subject of import relief unless 2 years have elapsed. Thus, the nonrubber footwear industry cannot seek import relief again until July 1, 1983. The safeguards in the proposed legislation do not change this. A lot can happen in the interim and we have absolutely no avenue of relief open to us and no way to redress injury caused by increased imports from the Caribbean. In this industry in particular we have watched as imports from developing countries increased rapidly. Imports of shoes from Hong Kong are a case in point and, even more recently, imports from the People's Republic of China. We have no reason to believe that Haiti, or the Dominican Republic, or any of the other Caribbean Basin countries will not be the next developing country to enter the U.S. market in a big way. Imports of nonrubber footwear from Haiti, for example, jumped from 774,000 pairs in 1980 to 1.2 million pairs in 1981, an increase of 55 percent in just one year. The reason for our concerns should be eminently clear.

Workers in the shoe industry and the other leather-related industries must be spared from any further import injury which is likely to result if imports from the Caribbean receive duty-free treatment. Shoes and leather-related products must be excluded from the free trade provisions of the CBI.

STATEMENT OF LEROY WEINER, PRESIDENT, LUGGAGE AND LEATHER GOODS MANUFACTURERS OF AMERICA, INC., AND PRESIDENT, AIRWAY INDUSTRIES, INC., ELLWOOD CITY, PA.

Mr. **Weiner.** My appearance before the subcommittee today is in my dual capacity as president of the Luggage and Leather Goods Manufacturers of America, Inc., the trade association representing domestic producers of luggage and personal leather goods, and as president of Airway Industries, Inc., a luggage company located in Ellwood City, Pa.

The industries which comprise this sector share the traits of labor intensity and import sensitivity, characteristics which are also shared with the textile and apparel industry.

I will confine my remarks today primarily to the anticipated negative effects of this Caribbean Basin Initiative on the luggage and personal leather goods industry. The luggage industry has been adversely affected by rapidly increasing imports of luggage, especially since 1975. Imports increased by a staggering five-fold times between 1975 and 1980, from $49 million to $243 million during a time when the real growth in the domestic market for luggage was only moderate, at best.

The industry estimates that the import penetration in 1980 was at least 36 percent. We also believe that even this estimate of 36 percent considerably understates the actual level of penetration in terms of quantity.

On top of this already major penetration, 1981 imports increased by 20 percent to $292 million and captured an even greater share of the U.S. luggage market, while domestic shipments during the same period of time declined. It is already evident that increasing imports are at the expense of domestic producers.

The situation with regard to personal leather goods is similar. The term "personal leather goods" or "flat goods" includes such products as billfolds, key cases, eyeglass cases, and coin purses of leather and other materials. In real terms, domestic shipments of personal leather goods have fallen since 1978, while imports have risen rapidly and captured at least 25 percent of the U.S. market by 1980.

Imports further increased by 17 percent to $84 million in 1981, and clearly captured an even larger share of the U.S. market at the same time as domestic production and shipments went flat. As with the luggage industry, imports of flat goods have been increasing at a time when the market has not been growing, and thus imports are at the expense of domestic production.

While import penetration in the personal leather goods industry has not yet reached the level achieved in the luggage industry, it is clear that the import market share is rising rapidly.

These two industries have been fighting an uphill battle literally for self-preservation. Last year the luggage industry sought and received a technical assistance grant of just under $250,000 from the U.S. Government designed to aid such import-impacted industries. We as an industry have embarked on an extensive and ambitious campaign to improve our productivity, produce an even higher quality product, offer better value to the consumer, and in general become more competitive.

With imports continually rising and no end in sight, and in light of the current depressed state of the industry, it should be clear why we are so fearful of the free trade aspects of the Caribbean Basin Initiative. Quite simply, these import-sensitive and battered industries cannot afford the further loss of market share which will undoubtedly occur if duty-free status is granted to imports from the Caribbean.

New foreign suppliers of imports to the United States do not displace traditional suppliers. Rather, they add to the already too vast pool of imports. We have seen this happen numerous times as new country suppliers enter the U.S. leather products market, clearly at the expense of domestic producers. We do not want to see this happen again.

With regard to the Caribbean Basin at a time when total U.S. imports of luggage and personal leather goods combined increased by 19 percent between 1980 and 1981, imports of these same products from the Caribbean increased by 61 percent. Even without duty-free status, imports from the Caribbean are growing at a faster rate than overall imports coming into the United States in these product categories.

I would also like to comment on the so-called safeguard measures available as part of the Caribbean Basin Initiative. A vivid illustration of the phenomenon of rapidly increasing imports is easily found if we study the imports of luggage.

In November 1981, 1 month alone, imports of luggage increased by 50 percent compared to imports in the same month in 1980. A situation of rapidly rising imports is already at hand for our industries, rendering future safeguards meaningless. Moreover, to bring such actions is time consuming and costly, an expense our industries and our members simply cannot afford.

Last year when there were several petitions which were accepted for GSP consideration with respect to luggage and personal leather goods, I had occasion to appear in person at hearings on two separate instances in Washington, and we filed innumerable documents and letters. The cost in time involved, of course, would be substantially magnified if we had to prove injury from Caribbean imports under the escape clause procedures. This is an unacceptable burden for us and is, in fact, no safeguard.

I have only one other comment I wish to make. I strongly believe that we are part of the foundation of the U.S. economy. As many as two out of three new jobs are created by small business. Airway Industries is a small business, but we happen to be the third largest employer of workers in our section of Pennsylvania.

We are also the employer of last resort for minorities and women. Airway employs three times on a percentage basis the number of racial minorities who reside in Lawrence County, and this county is suffering a current unemployment rate of 14.8 percent.

The negative effects of the CBI are going to be felt most strongly and most devastatingly on industries made up of small business and in communities such as ours. We are already suffering from the effects of import competition. Enough is enough. Do not make the leather products industries and the small businesses that make up these industries pay for this initiative.

Leather-related products must be excluded from duty-free treatment under the CBI. We urge you to add our products to the exclusion being granted to textiles and apparels.

Thank you for providing this opportunity to appear.

[The prepared statement follows:]

STATEMENT OF LEROY WEINER, PRESIDENT, LUGGAGE AND LEATHER GOODS MANUFACTURERS OF AMERICA, INC., AND PRESIDENT, AIRWAY INDUSTRIES, INC., ELLWOOD CITY, PA.

My name is Lee Weiner. My appearance before the Subcommittee today is in my dual capacity as President of the Luggage and Leather Goods Manufacturers of America, Inc., the trade association representing domestic producers of luggage and personal leather goods, and as President of Airway Industries, Inc., a luggage company located in Ellwood City, Pennsylvania. In addition, I am appearing as part of a coalition of leather products industries which is supportive of the basic objectives of the Caribbean Basin Initiative but whose goal is to seek an exclusion of their products from the free-trade aspects of the CBI.

The industries which comprise this sector share the traits of labor-intensity and import-sensitivity, characteristics which are also shared with the textile and apparel industry. We fell quite strongly that our products should receive an exclusion from duty-free treatment under the CBI similar to the exclusion being granted textiles and apparel.

I will confine my remarks today primarily to the anticipated negative effects of the CBI on the luggage and personal leather goods industries. First, let me provide you with some background information on these industries.

The domestic luggage industry has been adversely affected by rapidly increasing U.S. imports of luggage, especially since 1975, as imports have captured an increasingly large share of the U.S. market. In the past few years, domestic shipments of luggage have been on a decidedly downward trend, while imports have relentlessly increased. Imports increased five-fold between 1975 and 1980, from $49 million to $243 million, during a time when real growth in the domestic market was only moderate, at best. The industry estimates that import penetration in 1980 was at least 36 percent. This figure is based on U.S. Government data, which are available only on a value basis, and an estimate which takes into account insurance and transportation costs, duties paid, and a mark-up on imports to bring the import value to a point in the U.S. distribution system equivalent to the wholesale level of U.S. shipments. We believe that even this estimate of 36 percent import penetration considerably understates the actual level of penetration in terms of quantity. Moreover, in 1981 imports increased by 20 percent to $292 million and captured an even greater share of the U.S. luggage market, while domestic shipments declined. It is already evident that increasing imports are at the expense of domestic production.

The situation with respect to personal leather goods is similar. The term "personal leather goods" of "flat goods" includes such products as billfolds, key cases, eyeglass cases, and coin purses of leather and other materials. In real terms, domestic shipments of personal leather goods have fallen since 1978, while imports have risen rapidly and captured, according to our estimates, at least 25 percent of the U.S. market by 1980. Imports increased further by 17 percent to $84 million in 1981 and clearly captured an even larger share of the U.S. market. As with the luggage industry, imports of flat goods have been increasing at a time when the market has not been growing and, thus, imports are at the expense of domestic production. While import penetration in the personal leather goods industry has not yet reached the level achieved in the luggage industry, it is clear that the import market share is rising rapidly.

These two industries have been fighting an uphill battle for self-preservation. We have sought exclusion for our products from the Generalized System of Preferences on the grounds of import-sensitivity. Last year, the luggage industry sought, and received, a technical assistance grant of just under $250,000 from the U.S. Government designed to aid import-impacted industries. We have embarked on an extensive and ambitious campaign to improve our productivity, produce an even higher quality product, offer a better value to the consumer, and, in general, become more competitive.

With imports continually rising and no end in sight, and in light of the current state of the industry, it should be clear why we are so fearful of the free-trade aspects of the CBI. Quite simply, these import-sensitive industries cannot afford the further loss of market share which will undoubtedly occur if duty-free status is granted to imports from the Caribbean.

I would like to bring to the attention of the members of the Subcommittee a fact with regard to the import situation which is too often overlooked in the desire of the United States to help developing countries. New foreign suppliers of imports to the United States do not displace traditional suppliers; rather they add to the already too vast pool of imports. In other words, increased imports of luggage or personal leather goods from the Caribbean will not be at the expense of other imports, for example, from the Far East, but will instead be at the expense of domestic producers. We have seen this happen numerous times as new country suppliers enter the U.S. leather products markets. We do not want to see this happen again. The United States imported almost $5 million of luggage and personal leather goods from the Caribbean in 1981, a figure which is already on the rise. At a time when total U.S. imports of luggage and personal leather goods combined increased by 19 percent between 1980 and 1981, imports of these products from the Caribbean increased by 61 percent. Even without cutting the duties, imports from the Caribbean are growing at a faster rate than overall imports.

The rules of origin in the CBI are also cause for concern. If leather products are granted duty-free treatment under the CBI, a measure we strongly oppose, I expect that we will see products originating in the East or elsewhere shipped through the Caribbean either for finishing or even as transshipments to reap the benefits of duty-free access to the U.S. market. But there should be no misunderstanding of our position: we do not consider an increase in the local content level to be a solution to the terrible problems we will face if duty-free access to the U.S. market is permitted for our products.

I would also like to comment on the so-called safeguard measures available as part of the CBI. They will not work. They have not worked since the Trade Act of 1974 revised the "escape clause" procedures. During the six months that the International Trade Commission is investigating and the two months the President is considering what the ITC may recommend, imports will increase rapidly. This has been the case all too often since 1974. A vivid illustration of this phenomenon of rapidly increasing imports is easily found. Imports of luggage, in one month alone (November 1981) increased by 50 percent compared to imports in the same month in 1980. The situation of rapidly rising imports is already at hand, rendering future safeguards meaningless. Moveover, to bring such actions is time-consuming and costly, an expense our industries simply cannot afford. As it is now, these industries must repeatedly prove their import-sensitivity to the Executive Branch. Last year, when several petitions were accepted for GSP consideration with respect to luggage and personal leather goods, I had to appear in person at hearings on two separate occasions in Washington and we filed innumerable documents and letters. The cost and time involved, of course, would be substantially magnified if we had to prove injury from Caribbean imports under the "escape clause" procedures. This is an unacceptable burden for us and is, in fact, no "safeguard."

I have only one other comment I wish to make. I am disturbed regarding apparant inconsistencies between the anticipated effects of the CBI on industries such as these and the President's recent statement on small businesses. I believe he called us the "heart and soul" of the free enterprise system. I strongly believe that we are part of the foundation of the U.S. economy. Two out of three new jobs are created by small business. Airway Industries is a small business, but we are the third largest employer of workers in our section of Pennsylvania. We are also the employer of last resort for minorities and women. Airway employs three times, on a percentage basis, the number of racial minorities who reside in Lawrence County. And this county is suffering a current unemployment rate of 14.8 percent. The negative effects of the CBI are going to be felt most strongly and most devastatingly on industries made up of small business such as ours. In many cases we are already suffering from the effects of import competition. Enough is enough. Do not make the leather products industries and the small businesses of these industries pay for this policy initiative.

Leather related products must be excluded from duty-free treatment under the Caribbean Basin Initiative. We ask you to add our products to the exclusion being granted textiles and apparel.

Mr. **NEHMER**. Mr. Ralph Cennamo of New York City.

STATEMENT OF RALPH CENNAMO, GENERAL SECRETARY-TREASURER, INTERNATIONAL LEATHER GOODS, PLASTICS, AND NOVELTY WORKERS' UNION, AFL-CIO

Mr. CENNAMO. I am the general secretary-treasurer of the International Leather Goods, Plastics and Novelty Workers' Union, AFL-CIO. Our union represents a substantial number of workers in the domestic handbag, luggage, and personal goods industries.

All three of the industries in which our members work are labor intensive and thus particularly vulnerable to import competition from low-wage foreign countries. A large proportion of our workers are minorities, blacks or Hispanics, and a similarly large portion are women.

Most of our workers can be characterized as unskilled or semiskilled. Thus, many of our workers fall into the hard-to-employ category. Increasing volumes of imports are an ongoing concern of workers in these labor-intensive industries.

We have seen 75 percent of the U.S. market for handbags overrun by imports, and this is only over the last few years, and it looks like the U.S. industry could be wiped out completely. Thousands of jobs have been eliminated in this industry.

Import penetration is estimated at 36 percent in the luggage industry and 25 percent in the personal leather goods industry. Any added impetus to increasing imports, such as duty-free treatment for imports from the Caribbean, has a strong potential for further adversely affecting all three of these industries.

Our workers cannot tolerate any further erosion of their market or their job opportunities. Our union has consistently protested that these products are import sensitive and has fought against the inclusion of these products from duty-free treatment under the generalized system of preferences. Similarly, they should be excluded from duty-free treatment under CBI.

These three industries combined have traditionally employed more than 50,000 workers. According to Government data, some 4,000 jobs have been eliminated in the last 5 years alone. This is, I believe, a substantial understatement of the dire employment situation which exists in these industries.

Between 1979 and 1980, for example, 25 handbag factories closed, resulting in the loss of almost 3,000 jobs. Since that time, numerous additional plants have closed and even more workers are out of jobs. Let me add here that since 1982 many of our plants are working at half staff with many, many layoffs in the jobs remaining.

We have great difficulty competing with imports from low-wage countries such as those in the Caribbean. The average hourly wage in the domestic leather products sector was $4.99 in 1981, substantially below the average of $7.98 for all U.S. manufacturing, yet wages in certain of the Caribbean countries range from only 50 cents per hour to $2 per hour.

Developing countries have succeeded in gaining market share for the items our members produce, and clearly they do not need duty-free treatment to assist their U.S. market penetration any further. To allow duty-free entry of these imports will act only to increase the advantage of imports at the expense of domestic production and jobs.

The United States cannot export all the jobs of labor-intensive industries. If we allow this to happen, what will happen to these workers? Trade adjustment assistance benefits for workers who have lost their jobs because of imports have been drastically reduced.

I have not heard of anything that the administration is going to do to help those of our workers who will surely lose their jobs if the CBI bill is passed as proposed by the administration. I can tell you, though, what will happen. I do not expect many workers to find jobs elsewhere. Jobs lost will be permanent. The welfare rolls will increase. Isn't it enough that 9 million people are already out of work in this country?

We would like to see our neighbors and fellow workers in the Caribbean enjoy some economic, political, and social stability; however, why should our workers in the handbag, luggage, and personal leather goods industries be made to pay for this policy in disproportion to other U.S. industries?

The only satisfactory solution would exclude leather-related products from duty-free treatment just as it will exclude textiles and apparel. I urge you to grant this exclusion.

Thank you.

[The prepared statement follows:]

STATEMENT OF RALPH CENNAMO, GENERAL SECRETARY-TREASURER, INTERNATIONAL LEATHER GOODS, PLASTICS, AND NOVELTY WORKERS' UNION, AFL-CIO

My name is Ralph Cennamo and I am General Secretary-Treasurer of the International Leather Goods, Plastics, and Novelty Workers' Union, AFL-CIO. Our Union represents a substantial number of workers in the domestic handbag, luggage and personal leather goods industries. My appearance here today, as with the other spokesmen of the leather products industries, is to seek an exclusion of leather-related products from duty-free treatment under the Caribbean Basin Initiative. The exclusion we seek is the same as that being accorded textile and apparel imports.

All three of the industries in which our members work—handbags, luggage and personal leather goods—are labor-intensive and thus particularly vulnerable to import competition from low-wage foreign countries. Whether handbags, luggage, or personal leather goods, each of these industries has been characterized by increasing imports which have cause lost market share and jobs. A large proportion of our workers are minorities, primarily blacks and Hispanics, and a similarly large portion are women. In fact, many of our workers came to the United States from the Caribbean. Most of our workers can be characterized as unskilled or semiskilled. Mobility is limited. Thus, many of our workers fall into the "hard-to-employ" category.

Increasing volumes of imports are an ongoing concern of workers in these labor-intensive industries. We have seen 75 percent of the U.S. market for handbags overrun by imports. Thousands of jobs have been eliminated in this industry. While trends in the luggage and personal leather goods industries have not reached such dramatic proportions, they are nevertheless likewise suffering from import competition. Import penetration is estimated at 36 percent in the luggage industry and 25 percent in the personal leather goods industry. Any added impetus to increasing imports, such as duty-free treatment for imports from the Caribbean, has a strong potential for further adversely affecting all three of these industries. Our workers cannot tolerate any further erosion of their market or their job opportunities.

Our Union has consistently protested that these products are import-sensitive and has fought against the inclusion of these products from duty-free treatment under the Generalized System of Preferences. Similarly, they should be excluded from duty-free treatment under the CBI.

These three industries combined have traditionally employed more than 50,000 workers. According to Government data, some 4,000 jobs have been eliminated in the last five years alone. This is, I believe, a substantial understatement of the dire employment situation which exists in these industries. Between 1979 and 1980, for example, 25 handbag factories closed, resulting in the loss of almost 3,000 jobs. Since that time, numerous additional plants have closed and even more workers are out of jobs. More than 5,000 workers in handbag firms and an additional 2,000 in the luggage industry have been certified for trade adjustment assistance benefits by the U.S. Department of Labor because of unemployment or underemployment resulting from imports.

We have great difficulty competing with imports from low-wage countries, such as those in the Caribbean. The average hourly wage in the domestic leather products sector was $4.99 in 1981, substantially below the average of $7.98 for all U.S. manufacturing. Yet wages in certain of the Caribbean countries range from only $.50 per hour to $2.00 per hour. Developing countries have succeeded in gaining market share for the items our members produce and clearly they do not need duty-free treatment to assist their U.S. market penetration any further. To allow duty-free entry of these imports will act only to increase the advantage of imports at the expense of domestic production and jobs. The United States cannot export all the jobs of labor-intensive industries. If we allow this to happen, what will happen to these workers?

Trade adjustment assistance benefits for workers who have lost their jobs because of imports have been drastically reduced. I have not heard of anything that the Administration is going to do to help those of our workers who will surely lose their jobs if the CBI bill is passed as proposed by the Administration. I can tell you though, what will happen. I do not expect many workers will find jobs elsewhere. Jobs lost will be permanent. The welfare rolls will increase. Isn't it enough that 9 million people are already out of work in this country?

We would like to see our neighbors and fellow workers in the Caribbean enjoy some economic, political and social stability. However, why should our workers in the handbag, luggage and personal leather goods industries be made to pay for this policy in disproportion to other U.S. industries? The only satisfactory solution would exclude leather related products from duty-free treatment just as it will exclude textiles and apparel. I urge you to grant us this exclusion.

STATEMENT OF RICHARD MILLER, PAST PRESIDENT, NATIONAL HANDBAG ASSOCIATION, AND PRESIDENT, HARRY LEVINE CORP.

Mr. MILLER. Mr. Chairman, I am Richard Miller, president of the Harry Levine Corp., a ladies handbag manufacturer in New York City, past president of the National Handbag Association and a member of its board of directors.

I am also getting a little nearsighted, so I am going to read a little bit of this and then I would like to bring up a few other matters if I may.

Our goal is to gain an exclusion for leather-related products, including handbags, from the one-way-free proposal embodied in the Caribbean Basin Initiative. As a labor-intensive, import-sensitive industry, the results will be potentially devastating if these products are granted duty-free treatment.

Few industries have been as severely buffeted by import competition as has the U.S. handbag industry; 75 percent of the handbags sold in these United States are not made in these United States. And where it says here that the industry has experienced a loss of over one-fourth of all manufacturing plants, the latest number is that it is closer to one-third, and that we have lost about 45 percent of our labor force.

We have seen imports grow from 40 million units, valued at $45 million in 1967, to 144 million units valued at $351 million in 1980. Import penetration has grown from 29 percent in terms of quantity in 1967 to 75 percent in 1980. It is difficult to identify another U.S. industry which controls less than 25 percent of its own markets.

Within the leather products sector imports of handbags from the Caribbean are the most substantial at $14 million in 1981. The Dominican Republic and Haiti are the major suppliers of handbags from the Caribbean. Countries such as these do not need duty-free treatment to penetrate the U.S. market. Their domestic industries are developing quite rapidly without the additional aid of duty-free treatment.

For example, imports of all types of handbags from Haiti grew from just 745,000 units valued at $1.6 million in 1979 to 2 million units valued at $6.3 million in 1981. We expect to see imports from the Caribbean increasing rapidly over the next several years.

A couple of points of departure. I could not help but look at the position of President Reagan when he was talking about our good friends to the north and our good friends to the south. That is Mexico and that is Canada.

A gentleman from Mexico City came to me and wanted some information concerning suppliers. I gave it to him. He looked at the merchandise and said, well, why do we not export some of our bags from here to Mexico? I said, it sounds good to me, we are in business to do business. I said, what is the effective duty? He said about 92 percent. I said, how are you going to sell our bags at 92 percent. He said, you ship them 100 dozen and you bill them for 50 dozen, and that is the way they do business. That we did not do.

On the other side, Canada has had an excise tax. It is a Federal excise tax which one pays the duty, the prevalent duty, the GATT duty, on top of. In other words, if it is 20 percent, they have the duty that you pay on the initial first cost and you pay all those other costs. So in effect if a bag retails for $10 here in the United States, it will retail for $12 in Canada.

We make sure that we eliminate ourselves from exporting. Well, what about importing? When I was president of the association I was responsible for getting the largest countervailing duty ever against Brazil. It was not because I was the smartest. It was simply because they took a fledgling industry and supported it very, very directly. Very shortly after that Secretary of the Treasury Simon unilaterally shut that down by agreeing about submarine bases, and he did not know a French cuff from a rail frame, but he made sure he sold us down the river. The countervailing duty was eliminated.

The handbag industry has gone a long way down. We have taken care of the imports and we have taken care of the exports. We are not the United Auto Workers. We do not have nine personal holidays to give up. When I say "we" I mean the union that Ralph represents. We do not have one personal holiday for our workers. We do not earn half of what the United Auto Workers earn, less than half.

And we do not have a Douglas Fraser who comes back from Japan after trying to negotiate having plants built here saying, it is not a question of whether we are going to have a 4-day week, it is when. The handbag industry is willing to work 6 days a week, given an opportunity.

President Reagan said in his position paper, "free men working." Whenever anybody has wanted to penetrate the handbag industry, they have had no difficulty with the present existing duties. Now what we want to do is give some other people incentives so that those of us who have shops here in America cannot go in the shop and look anybody in the eye, because then we have to lay them off.

I thank you for your time.

[The prepared statement follows:]

STATEMENT OF RICHARD MILLER, PAST PRESIDENT, NATIONAL HANDBAG ASSOCIATION, AND PRESIDENT, HARRY LEVINE CORP.

Members of the Trade Subcommittee, I am Richard Miller, President of Harry Levine Corporaton, a producer of women's handbags located in New York City. I am also a member of the Board of Directors and past President of the National Handbag Association, the trade association representing the handbag industry. I want to thank you for the opportunity to appear here today as a representative of this industry.

Our goal is to gain an exclusion for leather-related products, including handbags, from the one-way free proposal embodied in the Caribbean Basin Initiative. As a labor-intensive, import-sensitive industry, the results will be potentially devastating if these products are granted duty-free treatment.

Few industries have been as severely buffeted by import competition as has the U.S. handbag industry. Over the last fifteen years, the industry has experienced a loss of over one-fourth of all manufacturing plants, despite modest growth in U.S. market demand for handbags. We have seen imports grow from 40 million units valued at $45 million in 1967 to 144 million units valued at $351 million in 1980. Import penetration has grown from 29 percent in terms of quantity in 1967 to 75 percent in 1980. We believe that with a further 16 percent increase in the quantity of imports in 1981 (to $406 million) imports now have an even higher share of the U.S. market. It is difficult to identify another U.S. industry which controls less than 25 percent of its own market.

Within the leather products sector, imports of handbags from the Caribbean are the most substantial at $14 million in 1981. The Dominican Republican and Haiti are the major suppliers of handbags from the Caribbean. Countries such as these do not need duty-free treatment to penetrate the U.S. market. Their domestic industries are developing quite rapidly without the additional aid of duty-free treatment. For example, imports of all types of handbags from Haiti grew from just 745,000 units valued at $1.6 million in 1979 to 2.0 million units valued at $6.3 million in 1981. This growth is typical of the growth in foreign labor-intensive industries and their exports to the United States. It is relatively easy to set up a handbag factory. Capital investment is relatively low and the Caribbean countries clearly have a large pool of cheap labor. As it is, we expect to see imports of handbags from the Caribbean increase over the next several years. Duty-free treatment will result in even greater increases in imports.

I am not convinced that the safeguard measures available to protect domestic industries will work. First of all, as I just described, imports can increase so rapidly that an injury investigation will take too long. And as these imports are increasing so fast, the domestic market is inundated by a new wave of imports. Imports from the Caribbean will not substitute for other imports. They will add to the import growth already occurring. A second factor that cannot be overlooked is the substantial cost involved for domestic industries in pursuing import relief cases.

The types of handbags currently being imported from the Caribbean are primarily of leather and plastic materials. Let me make it clear, however, that every imported handbag competes directly or indirectly with handbags produced in the United States. The nature of these products make them interchangeable with other similar products. Thus, a handbag of textile material can be substituted for a vinyl handbag. As a result, any increase in imports of any type of handbag, such as will occur if duty-free treatment is accorded imports from the Caribbean, will result in an increase in aggregate imports of these products and a subsequent loss of market share production and jobs. This is a very real concern to us, considering the market share and jobs already lost to imports.

The National Handbag Association urges this Subcommittee to exclude handbags and leather-related products from duty-free treatment under the CBI.

Mr. NEHMER. Jack Casey will complete our presentation.

STATEMENT OF JOHN A. CASEY, PAST PRESIDENT, WORK GLOVE MANUFACTURERS ASSOCIATION, AND VICE PRESIDENT AND GENERAL MANAGER, GRANET, DIVISION OF WGM SAFETY CORP.

Mr. CASEY. Mr. Chairman and members of the Committee, my name is Jack Casey. I am vice president and general manager of the Granet Glove Company, and the immediate past president of the Work Glove Manufacturers Association in the United States.

Besides cotton work gloves, which are covered by the multifiber arrangement and thus excluded from the CBI, the members of the Work Glove Manufacturers Association produce gloves of such materials as leather, plastic, rubber, and coated fabric. It is for these leather and leather-related products that we are seriously concerned regarding the free trade aspect of the CBI. These products should be granted an exclusion similar to the textile and apparel-type gloves.

The work glove industry is composed primarily of small sized firms and is both labor intensive and import sensitive. Minorities are employed, both racial and women, which in fact compose more than 50 percent of our employees.

Imports of work gloves have increased both absolutely and relative to domestic shipments and consumption in recent years. Import penetration varies for the individual glove types and is highest for leather-fabric combination gloves, which registered an estimated 74 percent import market share in 1981.

Import penetration for the overall fabric, coated fabric as well as leather work glove, industry exceeds 40 percent. Even without duty-free status, imports of many of these products from the Caribbean have increased in recent years. With zero duty, clearly the increase in imports will be substantially greater and at a direct cost to the domestic firms and workers in the work glove and other leather-related industries. These industries simply cannot endure further inroads into the domestic market for their products.

I would like to comment on just two of the several items of concern regarding the CBI. First, with respect to the so-called safeguard mechanisms, I am particularly concerned that there is no path for an industry to pursue other than under the escape clause provisions. The work glove industry, despite its import sensitivity and the negative impact sustained as a result of increasing imports, was denied import relief under the escape clause when its petition was rejected by the International Trade Commission.

On a second occasion, in late 1977, the industry petitioned the ITC under section 406 of the Trade Act of 1974, claiming disruption of the cotton work glove market as a result of increased imports from the People's Republic of China. That petition was also denied.

Both of these efforts involved a significant expenditure of time, effort and considerable money on the part of our industry, which is a very small industry, and obviously it was to no avail. The turnaround time for such a case is simply too long. We do not believe that this route will work to truly safeguard industries such as ours against injury resulting from increased imports from the Caribbean.

Second, with respect to the recent posture taken by the Administration with respect to small business, I am distressed that the President has not recognized the apparent contradiction in terms. On the one hand, small businesses are important to the U.S. economy and President Reagan has pledged his support to them. On the other hand, however, it is clear to us that domestic industries comprised of small businesses, such as the leather and leather substitute products sector, are likely to play the part of the losers at the hands of a policy such as the CBI.

The one-way free trade proposal of the CBI is not consistent with the policy toward small businesses. Nor is it consistent with the dire employment situation which currently exists in this country.

Someone mentioned earlier, we have worked short time in the glove industry. For the last 3 years our employment has dropped 25 percent. We cannot deny the need for a policy to help the Caribbean nations. We are just not willing to pay more than our fair share.

An amendment to the Caribbean Basin Initiative must be made that excludes work gloves and other leather-related products from duty-free treatment. Such an amendment is the only equitable solution.

Thank you, Mr. Chairman.

[The prepared statement follows:]

STATEMENT OF JOHN A. CASEY, PAST PRESIDENT, WORK GLOVE MANUFACTURERS ASSOCIATION, AND VICE PRESIDENT AND GENERAL MANAGER, GRANET, DIVISION OF WGM SAFETY CORPORATION, FRAMINGHAM, MASS.

Members of the subcommittee, my name is John Casey, Vice President and General Manager of Granet, a division of WGM Safety Corporation, a producer of work gloves located in Framingham, Massachusetts. I am also past President of the Work Glove Manufacturers Association, a trade association whose members account for the great bulk of the domestic output of work gloves.

Among the industries of the leather products sector which are seeking an exclusion for their products from duty-free treatment under the Caribbean Basin Initiative, our industry is in a slightly unique position. Some of the work gloves produced by this industry are of cotton textile materials and, in that sense, we are part of the textile and apparel complex. Thus, our cotton work gloves will be excluded, along with textiles and apparel, from duty-free treatment under the Caribbean Basin Initiative. Although cotton work gloves are covered by the Multifiber Arrangement (MFA), other work gloves do not benefit from any restraints on imports. Our manufacturers also produce gloves of such materials as leather, plastic, rubber, or coated fabrics, none of which is covered by the textile and apparel exclusion. It is for these leather and leather-related products that we are seriously concerned regarding the free trade aspects of the CBI. These products should be granted an exclusion similar to textiles and apparel.

The work glove industry, like the other industries in this sector, is composed primarily of small-sized firms and is both labor-intensive and import-sensitive. Minorities, both racial and women, comprise a major portion of our work force.

Imports of work gloves have increased both absolutely and relative to domestic shipments and consumption in recent years. Import penetration varies for the individual glove types and is highest for leather/fabric combination gloves which registered an estimated 74 percent import market share in 1981. Import penetration for the overall fabric, coated fabric and leather work glove industry exceeds 40 percent.

We share a deep concern with the other leather-related industries regarding duty-free treatment for products imported from the Caribbean. Even without duty-free status, imports of many of these products from the Caribbean have increased in recent years. *With* zero duty, clearly the increase in imports will be substantially greater and at a direct cost to firms and workers in the work glove and other leather-related industries. These industries simply cannot endure further inroads into the domestic market for their products.

First, with respect to so-called safeguard mechanisms, I am particularly concerned that there is no path for an industry to pursue other than under the "escape-clause" provisions. The work glove industry, despite its import-sensitivity and the negative impact sustained as a result of increasing imports, was denied import relief under the "escape clause" when its petition was rejected by the International Trade Commission. On a second occasion, in late 1977, the industry petitioned the ITC under Section 406 of the Trade Act of 1974 claiming disruption of the cotton work glove market as a result of increased imports from the People's Republic of China. That petition was denied as well. Both of these efforts involved a significant expenditure of time, effort, and money on the part of our industry, to no avail. The turnaround time for such a case is simply too long. We do not believe that this route will work to truly safeguard industries such as ours against injury resulting from increased imports from the Caribbean.

Second, with respect to the recent posture taken by the Administration with respect to small businesses, I am distressed that the President has not recognized the apparent contradiction in terms. On the one hand, small businesses are important to the U.S. economy and President Reagan has pledged his support to them. On the other hand, however, it is clear to us that domestic industries comprised of small businesses, such as the leather and leather-related (or leather substitute) products sector, are likely to play the part of the losers at the hands of a policy such as the CBI.

The one-way free trade proposal of the CBI is not consistent with the policy toward small businesses. Nor is it consistent with the history of trade legislation and trade policy which has preceded it. Nor is it consistent with the dire employment situation which currently exists in this country. We cannot deny the need for a policy to help the Caribbean. We are just not willing to pay more than our fair share of the burden generated by such a policy.

An amendment to the Caribbean Basin Initiative must be made that excludes work gloves and other leather-related products from duty-free treatment. Such an amendment is the only equitable solution.

Mr. NEHMER. Mr. Chairman, that completes our presentation. I just wanted to add one point, that the Footwear Industries of America has submitted its testimony to you. They would be here today except for the fact that they have their annual meeting going on at this time outside of Washington.

We stand ready to answer any questions.

[The prepared statement referred to follows:]

STATEMENT OF FAWN K. EVENSON, FOOTWEAR INDUSTRIES OF AMERICA

INTRODUCTION AND SUMMARY

Footwear Industries of America (FIA) is a trade association representing domestic manufacturers of nonrubber footwear and suppliers to the footwear industry. We are pleased to have the opportunity to comment on the Administration's Caribbean Basin Initiative (CBI) proposal.

FIA recognizes the need to promote economic and political stability in the Caribbean region. However, we are concerned that duty-free imports of footwear from Basin countries, under the one-way free trade provisions of the CBI, will unfairly burden firms and workers in our industry. Imports already account for 51 percent of the nonrubber footwear market; if Caribbean Basin beneficiaries are encouraged to export duty-free footwear to the U.S., footwear imports could grow dramatically, further threatening the domestic industry.

Therefore, we recommend that footwear be excluded from the list of products eligible for duty-free treatment from countries designated as beneficiaries of the Caribbean Basin Initiative.

BACKGROUND

It long has been recognized that footwear is among the most import-sensitive industries in the U.S. and that it continues to be severely threatened by high levels of imports. The Congress acknowledged the import-sensitive nature of footwear by including footwear in a list of articles specifically excluded from eligibility for Generalized System of Preferences (GSP) treatment under Title V of the Trade Act of 1974.

Further, the International Trade Commission (ITC) unanimously determined that imports seriously injured the domestic footwear industry. Following the second unanimous injury finding, import relief was grated to the industry in June, 1977, in the form of Orderly Marketing Agreements (OMA's) negotiated with Taiwan and Korea to limit imports from those two sources for four years (June 30, 1977–June 30, 1981).

In April, 1981, The ITC concluded that footwear imports continued to injure the domestic industry, and recommended extension of import quotas on footwear from Taiwan, the largest single foreign supplier. The ITC further recommended that action be taken against surges from other countries whose imports undermined the import relief program and threatened the domestic industry. On June 30, 1981, despite the ITC's recommendation, President Reagan terminated the Orderly Marketing Agreements with both Taiwan and Korea.

Prior to, during, and following termination of the relief program, imports continued to capture roughly one-half of the domestic nonrubber footwear market—the highest import penetration rate of any major industry, including automobiles or steel. After the termination of the import relief program, imports in 1981 exceeded 1980 levels by roughly 10 million pairs, despite a drop in consumption. In the face of rising imports, domestic production is estimated to drop by nearly 21 million pairs.

Injury to the industry could become even more severe if Caribbean Basin beneficiaries are encouraged to export duty-free footwear to the U.S. footwear exports from the area can be expected to grow dramatically

The Caribbean Basin Area clearly has the potential to develop its footwear industry. Footwear is considered an "easy-entry" industry; it is one of the earliest manufacturing industries encouraged by developing countries, because of their low-wages, and pool of semi-skilled labor. While current shipments from the region are only at 2 million pairs, historical trends indicate that a country can increase footwear exports substantially in a very short time period. For example:

Imports from Singapore grew from 1,000 pairs in 1977 to almost 4.5 million pairs last year.

Imports from Hong Kong rose from 8.7 million pairs to 22.1 million pairs between 1977 and 1979.

Imports from the Philippines rose from 620,000 pairs in 1977 to 14.3 million pairs in 1980.

Between 1977 and 1980, imports from Thailand grew from 120,000 pairs to 2.6 million pairs.

Before political problems disrupted its industry, imports from El Salvador rose from a mere 53,800 pairs in 1977 to 3.4 million pairs in 1979.

Second, numerous Caribbean countries already have an indigenous footwear industry. (See Table I, attached) Again, many still are relatively small, but comparatively low capitalization requirements make expansion of capacity easy. Thus, the potential exists for rapid expansion of production and exports if the U.S. offers these countries duty-free treatment on footwear.

It also must be noted that imports from the Caribbean will be in addition to already high imports from other sources. They will not merely replace existing suppliers. While there has been some historical displacement of imports from other suppliers as new sources develop, the predominant effect of higher imports has been to reduce domestic production, not total imports other nations.

For example, bertween 1968 and 1976, when imports from Taiwan and Korea rose by 183.7 million pairs, imports from the rest of the world did not decline; it was domestic production which fell by 220 million pairs, most of this due to the rise in imports. In addition, a number of relatively new entrants into the market have now gained a significant foothold in the U.S. It is unlikely that these now-established and growing suppliers to the U.S. market could be replaced or destroyed. Imports from Hong Kong, for instance, have held at over 20 million pairs (growing from 6.6 million in 1976), and at 28 million pairs in 1981, were 36 percent above year-earlier levels. Imports from the Philippines rose from almost nothing in 1976 to 14 million pairs in 1980. In fact, imports from the Philippines rose in 1980 in face of a general drop in consumption and imports. Singapore increased its imports from 2.9 million pairs in 1980 to almost 4.5 million pairs in 1981, a 50 percent growth, despite an overall growth rate in imports of 2.7 percent. Clearly these "new entrants" are not going to disappear from our market due to increased development in the Caribbean.

A further indication of the Caribbean area's potential to expand its footwear industry is the fact that the area is a major exporter of footwear uppers, as Tables II and III indicate. The Dominican Republic and Haiti are the second and third largest suppliers, respectively, of unlasted leather footwear uppers and of other (rubber/

plastic, cotton and fiber) uppers. In 1981, their combined imports of uppers were 9.4 million pairs. However, higher-value finished products may be shipped instead if footwear is afforded duty-free treatment.

Also, cotton and fiber uppers will not receive duty-free treatment because they are covered by the Multi-Fiber Agreement. However, if these uppers are converted into higher-value finished footwear, the finished product will enter duty-free under the CBI. We should also note that rubber/fabric footwear imports have duties ranging from 20 percent to an effective rate of 65 percent. Certainly, this is an incentive to convert these uppers to duty-free finished footwear.

The U.S. will be the focal point for Caribbean exports, since it is the largest and most open market in the world

U.S. tariffs on nonrubber footwear are among the lowest in the world, ranging from 0 to 20 percent ad valorem. The trade-weighted ad valorem rate is approximately 10 percent. In comparison, Canadian duties for countries with MFN status range from 22½ percent–25 percent ad valorem. In Korea, the general duty range is 60 percent ad valorem. Mexico's duty rate is 35 percent ad valorem FOB, plus additional surcharges and taxes. Spain's duties range from 8 percent–35 percent ad valorem, with an additional compensatory imports tax of 10 percent. Brazil has a 170 percent ad valorem tariff, in addition to a deposit scheme and additional taxes, which virtually prohibit footwear imports. Duties in Australia generally are 34 percent or 46.5 percent ad valorem. Duties in Japan range from 8.6 percent-27 percent. (Source: U.S. Department of Commerce)

Moreover, non-tariff barriers in the U.S. are virtually non-existent. (The one non-tariff barrier applicable to shoes, American Selling Price, was abolished on July 1, 1981.) In contrast, Canada has imposed a global quota (recently liberalized) on footwear imports. Mexico requires licenses on all footwear imports, which are not issued freely. In the Philippines, footwear is classified as a consumer item which cannot be imported. Brazil requires import licenses, which generally are not issued for footwear. Australia maintains quantitative restrictions on many types of footwear. Japan has a severe quota on imports of leather products which includes leather footwear.

It is not surprising, then, that U.S. imports accounted for 39 percent of total nonrubber footwear imports by OECD countries in 1976 and 1977 (the latest year for which such data are available). For most of the world's top 19 footwear exporting countries (which account for almost 85 percent of total world exports), the U.S. is the single largest recipient of footwear exports, absorbing 41 percent of total exports by these 19 countries.

We would also like to mention that our industry has been aggressively pursuing export markets for the past several years. We have expanded the value of exports from $35 million in 1977 to $120 million in 1981, an increase of almost 250 percent. We have focused our program to date on Europe, but are looking to the Caribbean and Latin America for export growth in the next few years as well. Government sponsored research on tariff and non-tariff barriers on our products in the Caribbean shows a remarkable array of disincentives to footwear exports—ranging from tariffs as high as 150 percent ad valorem, to quotas of one dozen pairs per type of shoe per year, to outright embargoes on footwear imports. While the Congress is considering "reciprocity" legislation, it is also considering, in the CBI, allowing duty free access to our market to some of the most restrictive markets in the world.

Safeguard measures are not sufficient to prevent substantial growth in imports

The Administration has proposed use of the "escape clause" procedure to safeguard domestic industries from injury under the Caribbean Basin Initiative. Nonrubber footwear, however, is precluded from even filing a petition under this safeguard mechanism until July of 1983.

Under the terms of the Trade Act of 1974, Section 203 (j):

"No investigation for the purposes of section 201 shall be made with respect respect to an article which has received import relief under this section unless 2 years have elapsed since the last day on which imports relief was provided with respect to such article pursuant to this section."

The import relief program for non-rubber was terminated by this Administration on July 1, 1981. According to our interpretation of the bill submitted to the Congress called the "Caribbean Basin Economic Recovery Act", no changes have been made to this section of the Trade Act of 1974. Thus, our industry, which was found injured by imports by the International Trade Commission as recently as last April, cannot even utilize the safeguard provisions of the CBI until July of 1983.

Further, while agricultural products have been given a "fast tract" mechanism for escape clause relief under the CBI, no such provision is included for other products. Thus, the full nine month time frame provided under section 201 of the Trade Act must elapse before relief can be provided. Assuming that our industry were to petition for relief in July of 1983, we would not even have a decision before March of 1974.

Given the growth in imports from various "new start" countries to which we have referred in previous sections of this testimony, this two year waiting period before import relief could be provided offers us little consolation.

Furthermore, the necessity of having to prove injury under the safeguard measures is a needleless and costly burden to the industry. The government already has a wealth of information on the injury to the industry from imports—from two affirmative ITC injury findings and the ITC recommendation last year that import relief not be terminated.

Finally, our recent experience with the Administration, which terminated our import relief program despite the recommendation of the International Trade Commission, leaves us with little confidence in the whole safeguard mechanism.

Other concerns about the Caribbean basin initiative

Another very serious problem we see with the CBI is that footwear from other sources may be transshipped through the Caribbean area or assembled there to take avantage of duty-free export to the U.S. The industry experienced a severe transshipment problem when footwear from Taiwan was transshipped through Hong Kong to avoid the quota on nonrubber footwear imports from Taiwan. The Administration acted on this problem only after it existed for several months. Almost seven months elasped from the time the issue was originally called to its attention, to the time that a Certificate of Origin program was implemented with Hong Kong in November, 1978. Thus, it was time-consuming to investigate and remedy the problem. In the meantime, the footwear industry developed in Hong Kong, and its imports have remained at high levels—over 20 million pairs.

It also is likely that production facilities may be transferred from the Far East to the Caribbean, to take advantage of the latter area's even lower wage rates and proximity to the U.S. market. Or with only a 25 percent local value content requirement, the Caribbean Basin could become a major "finishing" area for footwear essentially produced elsewhere, and then shipped to the U.S. duty-free.

Public policy considerations indicate that the Caribbean basin initiative could be counterproductive at this time

With unemployment hovering around 9 percent, development initiatives in the Caribbean area could result in the export of much-needed U.S. employment. Footwear workers would be severely affected, since they are among the hardest to employ and frequently experience prolong unemployment. They are generally women, under 25 or over 50 years of age, semi-skilled, and with limited formal education.

RECOMMENDATION AND CONCLUSION

The Congress must recognize the import-sensitive nature of the nonrubber footwear industry and the severe threat which imports continue to pose. Encouraging exports from the Caribbean Basin will only exacerbate the injury caused by already excessively high levels (51 percent penetration rate) of imports. Thus, footwear should be excluded from the items eligible for duty-free treatment from countries designated as beneficiaries of the Caribbean Basin Initiative.

TABLE 1.—NONRUBBER FOOTWEAR: U.S. IMPORTS FROM SELECTED CARIBBEAN COUNTRIES ANNUAL 1977-81

[In pairs]

	1977	1978	1979	1980	1981
Bahamas			19,656	361	342
Barbados					
Costa Rica	20,486	43,288	60,348	128,937	115,050
Dominican Republic	26,408	198,619	205,698	152,003	295,095
El Salvador	13,464	409,755	3,418,616	176,571	3,755
F W Indies	1,620			10,050	
Guatemala	99,968	167,254	145,936	287,227	334,025
Guyana		2,470	90	2,050	1,488
Haiti	598,894	701,128	626,630	774,251	1,197,835

TABLE 1.—NONRUBBER FOOTWEAR: U.S. IMPORTS FROM SELECTED CARIBBEAN COUNTRIES ANNUAL 1977-81—Continued

[In pairs]

	1977	1978	1979	1980	1981
Honduras		205	18,138	1,351	7,908
Jamaica	2,823		900	112	
LW/WW I				3,610	2,183
Antilles		84			30
Nicaragua	1,548				300
Panama		2,730	3,840	1,986	33,632
Surinam	44,268	6,766	1,680		5,056
Trinidad	337		7,308		
Total selected Caribbean countries	809,816	1,532,299	4,508,840	1,538,509	1,996,699

Source: Department of Commerce data.

TABLE 2.—RUBBER/PLASTIC, COTTON AND FIBER SHOE UPPERS BY COUNTRY

[In thousand pairs]

	1980	1981
Dominican Republic	3,304.0	4,280.1
Haiti	752.6	1,196.5
Hong Kong	910.3	755.3
El Salvador	231.0	348.5
Korea	96.0	59.5
Taiwan	3,575.3	5,505.8
Mexico	1,171.3	271.7
All other	245.7	697.6
Total world	10,286.2	13,115.0

Source: U.S. Department of Commerce, IM146.

TABLE 3.—UNLASTED LEATHER SHOE UPPERS BY COUNTRY, 1980 AND 1981

[In thousand pairs]

	1980	1981
Korea	4,591.0	3,449.3
Taiwan	915.7	1,240.4
Dominican Republic	2,294.8	2,269.2
Haiti	2,154.7	1,645.9
Mexico	782.8	1,065.5
India	390.4	1,210.9
Hong Kong	296.6	335.4
Brazil	103.9	211.7
El Salvador		18.9
All other	1,189.0	1,354.8
Total world	12,718.9	12,822.0

Chairman GIBBONS. I know you have waited a long time to be heard. I appreciate your coming.

Let me ask something that is perhaps not relevant to this, but I notice that a number of you are not only head of the union, but you are also head of the company, too—Mr. Miller, Mr. Weiner, and some others.

Mr. **Miller.** Ours is a trade association, and we elect the officers of the association.

Mr. **Weiner.** This is a trade association carried on by the individual member companies within the industry.

Mr. **Nehmer.** You have both the individual unions and the trade associations working together, and we are before you today, Mr. Chairman.

Chairman **Gibbons.** Well, I am sorry to see the very depressed status of your particular sector of the American economy. I know it is a real problem. And let me ask you —I ought to know, but I do not have it on the tip of my tongue—what the effective tariff rate is on imported leather products.

Mr. **Nehmer.** It varies by product, Mr. Chairman.

Chairman **Gibbons.** I realize that.

Mr. **Nehmer.** In luggage the range is from 6½ percent to 20 percent; in personal leather goods, from 6.1 percent to 20 percent; in the case of handbags, from 6½ percent to 20 percent; in the case of leather wearing apparel it is just 6 percent; in the case of nonrubber footwear it ranges from free—there are some limited products free—to 20 percent, but the trade-weighted average is 10 percent. In the case of work gloves it ranges from 4½ percent to 27 percent.

And I should point out that during the Multilateral Trade Negotiations the cuts in tariffs on these products were fairly limited, except in the work glove area where rubber gloves did have a 60 percent cut in the tariff. But the others by and large did not have their tariffs cut during the MTN.

Very few of these products, just a limited number, are on the GSP zero duty list. They have been excluded from that either by the Trade Act of 1974, which excluded footwear, or by the action of the executive branch.

Chairman **Gibbons.** What are the products that are in the high end? Is that the 20 percent range?

Mr. **Nehmer.** In the case of luggage and handbags, it is vinyl luggage and handbags.

Chairman **Gibbons.** That are in those very high——

Mr. **Nehmer.** That is right. In the case of nonrubber footwear, it is certain leather footwear that I can identify further.

Chairman **Gibbons.** OK. And despite those kinds of tariffs, you are still having severe problems in the industry, is that right?

Mr. **Nehmer.** Yes. It happens that the import growth, for example, on the luggage side has been heavier where the tariff has been lower. In other words, the recent increases in the luggage imports which Mr. Weiner referred to has not been as great where the tariff has been 20 percent as it has where the tariff has been 9 percent or somewhere in between.

Mr. **Weiner.** In answer to your question, one thing has been certain over the last 10 years. That is, the amount of imports has increased as well as their penetration in the market, regardless of what has happened to the growth of the market itself.

Chairman **Gibbons.** I assume this is because this is a labor intensive type of work and it is not a high technology component, nor is it a particularly high capital intensive type of work. Is that what we are talking about? Have I correctly described it?

Mr. **Weiner.** Yes.

Mr. **Nehmer**. In that respect, it meets the same criteria as the textile and apparel industries.

Mr. **Gundersheim**. If I could add a comment. Not to say that zero duties would have inconsequential effects, the fact that it might be 10 or 6 or 20 percent, it does have an effect of not totally overwhelming us on these import questions. We obviously consider it of significance; otherwise, we would not be here.

Chairman **Gibbons**. I would consider 20 percent to be a lot more effective than 3 or 6.

Mr. **Nehmer**. Leather wearing apparel had a duty of 6 percent. The duty went from 6 percent to zero because GSP benefits were granted that product, and in 1976 we saw a shooting up of imports from the different developing countries. And when 3 years later the duty of 6 percent was restored, leather good imports did decline; not the way it was before it went into effect, because the foreign suppliers already had a piece of the market which they did hold onto.

In that case we had to argue very strenuously that 6 percent made quite a lot of difference in the level of imports.

Mr. **Weiner**. One of the things that happened is that in most industries like this there is a very delicate balance. In our own case, the luggage industry, with a government grant that we have, we are going to be encouraging our members to develop a business strategy to make their operations more viable. During that period of time they are very vulnerable to any impact that might take place with regard to imports and this could be disruptive to the planning they are doing.

Mr. **Nehmer**. You know, Mr. Chairman, four of the industries here before you—luggage, handbags, nonrubber footwear and work gloves—all have received EDA grants, grants from the Department of Commerce, because they are import impacted, to assist them in improving their competitive position vis a vis imports.

And all of these programs are either just starting as in the case of luggage, a bit further along as in the case of work gloves, much further along in the case of handbags and nonrubber footwear, but they all are a result of a decision by the executive branch that these are import sensitive, import impacted industries. I would guess the Government's investment in these programs runs into several million dollars now.

So on the one hand we have the Government providing funds to improve the competitive position of these industries, and on the other hand the administration is proposing zero duty treatment which would include leather products, which could only have an adverse effect, just an opposite effect for these industries.

Chairman **Gibbons**. Do these countries generally produce the hides for their leather or do they import the hides?

Mr. **Nehmer**. Both. There is some production in the Central America-Caribbean area, but they also do import.

Mr. **Casey**. Mr. Chairman, just to point out the significance of the impact that zero duty has on products of our type, I would like to read the results of rubber gloves, which we are not here discussing, but nonetheless it is pertinent to our industry and germane to this particular subject.

In Malaysia in 1976 there were no imports in rubber gloves, but as you know Malaysia was given duty-free status as an underdeveloped country. In 3 years, in 1979, they imported 1,000,232 dozen pairs. It only took them 3 years to get a very high percentage or a good percentage of the market. So that the duty-free aspect of the CBI is of great concern, and we have evidence of that in this rubber glove business.

Mr. MILLER. Mr. Chairman, going back a few years on the GSP, Taiwan was one of the countries—and this is concerning handbags, and as I understand it the system of GSP was to encourage less developed countries to get going in a particular industry. At that time they were doubling the size of their industry about every 3 years. They had achieved significant market penetration.

And this is a little different case, but it is not much different. At least in handbags, if they are going to do us they are going to do us. But what we do not need is the Government giving us a hand and being done to. [Laughter.]

Chairman GIBBONS. That is good English.

Mr. Bailey?

Mr. BAILEY. Thank you, Mr. Chairman.

How many jobs do you people represent? Not just the employees you have working; how many businessmen are displaced, how many clerical, how many union people? Do you have any rough idea?

Mr. MILLER. We have about 16,000.

Mr. BAILEY. You sitting right here, all of you?

Mr. GUNDERSHEIM. No, no. The total industry, roughly a quarter of a million people.

Mr. BAILEY. Now let me ask you this: Would distribution channels change?

Mr. WEINER. That does not include the suppliers to those industries. It only includes the people gainfully employed in the production of the product.

Mr. BAILEY. If you were replaced entirely, would those people be absorbed? Who would be absorbed?

Mr. NEHMER. You mean of the other workers who are dependent upon this industry?

Mr. BAILEY. Yes.

Mr. NEHMER. Very few of them, I would assume, would be. The ratio is about—based upon what occurs in the textile and apparel industry, it is about 2 to 1. For every two workers directly employed, there is another worker in another industry.

Mr. BAILEY. Has the administration approached you people? You know, I assume that if market penetration approached 100 percent and you were displaced completely, you certainly would have to be affected more than to the tune of 250,000 workers. You have got transportation systems, distribution systems, already in place that would absorb the imports. You have to have some spinoff in terms of those 250,000 jobs.

Has anybody done any work on that?

Mr. NEHMER. The footwear industry only 10 years ago or less had almost as many workers, 250,000—I think it was 240,000 workers—as the entire leather products sector that we are talking about today. They have lost that employment, those jobs, to imports as the import penetration rose to 50 percent.

Mr. **Hrubes**. I was just going to add that the impact of these plant closings depends upon the location, and most of them are located in small towns.

Mr. **Bailey**. What part of the country?

Mr. **Hrubes**. Northeast. Pennsylvania, for example, has many of them that have closed already. Missouri in the Midwest.

Mr. **Bailey**. Missouri, let me write that down. That is a good State.

Mr. **Hrubes**. When these plants close, the town closes. There is no other employment. We have been recently notified of two closings, one in Missouri and one in Kentucky.

Mr. **Bailey**. Does not the Government do anything when they are notified of a closing? If the Government goes out and passes a trade policy that directly replaces your job, there is no just compensation for that, is there?

Mr. **Weiner**. No one has ever discussed with us the ramifications of decisions of this type. Basically, our conversations with people in Commerce and trade and in State have indicated that we should not be concerned about this particular situation, that we will not be affected, and there has been no discussion with regard to the ramifications—not only the impact on the people whom we have employed, but the ripple effect that would come from those people not being employed.

Mr. **Bailey**. You say that EDA is surety on these loans to help you modernize. Do we know how much those loans are?

Mr. **Nehmer**. We are talking about two different things here, sir. One is the industrywide program of technical assistance to four of the industries I mentioned. Those are not loans, they are technical grants for studies to improve the competitive position.

Mr. **Bailey**. But it represents an investment.

Mr. **Nehmer**. Yes, several million dollars, the biggest being for footwear.

In addition to that, individual firms in these different industries have received loans or loan guarantees under the trade adjustment assistance program.

Mr. **Bailey**. If they receive loans and loan guarantees under trade adjustment or readjustment or whatever assistance programs, and if EDA has been involved, how highly indebted is the industry? Does anybody know how leveraged it is?

Mr. **Nehmer**. To EDA? No, I do not think we have those data.

Mr. **Bailey**. Some of the businessmen are here. How does it operate? How does your business operate? Yes, sir.

Mr. **Casey**. Mr. Bailey, I would like to back up and then I will answer that question. We have a small plant in Snow Hill, N.C. We employ approximately 100 people. They are not working full time and they have not worked full time for 3 years. But we are the largest single payroll in Snow Hill, N.C. The people love us, they love the job. The community depends on us.

To answer your question more positively, it is a low investment industry. It is a sewing machine. It is the kind of business that will go to the Caribbean if they can get duty-free entries.

Mr. **Bailey**. You mean we are not going to be exporting tons of American capital equipment to the Caribbean? We are not going to be doing that?

Mr. **Casey**. No. That is just one of the fallacies in the CBI.

Mr. **Gundersheim**. If I could amplify. All the machinery used in this industry is produced abroad.

Mr. **Bailey**. Where?

Mr. **Gundersheim**. In Japan, in Europe, in a number of Asian countries, actually, in addition to Japan. You recall, Singer Sewing Machine just closed its last plant in the United States.

Mr. **Bailey**. When was that?

Mr. **Gundersheim**. Two months ago, in Elizabeth, N.J.

Mr. **Bailey**. Maybe you can discount the machinery and sell it back.

Mr. **Nehmer**. There is a lot of used equipment that is exported every year. What you are dealing with are cutting machines, sewing machines, pressing and forming machines.

These are commonly produced in developing countries and certainly exported in a used condition from countries like the United States.

Mr. **Bailey**. Do you have any figures on your capital replacement, how much of this equipment you buy from overseas?

Mr. **Nehmer**. Buy from overseas?

Mr. **Bailey**. Yes. Do you know how much?

Mr. **Nehmer**. Unless the import data have a breakout, which I doubt, on this industrial machinery that is used, I do not know. We could check that, Mr. Bailey, and supply it for you.

[The information follows:]

As was stated during the course of the hearing, we believe that most of the machinery and equipment utilized in these industries is produced abroad. There appear to be no data, however, on the amount of this equipment which is imported for use in the leather products industries.

Mr. **Bailey**. You have existing service industries that service this equipment. That would go, too. You have not factored that into the 250,000 jobs?

Mr. **Weiner**. None of the support for the industry is included in the 250,000.

Mr. **Nehmer**. Direct employment in these industries is about a quarter of a million, and you figure roughly 50 percent of that number is employed in other industries servicing this.

Mr. **Bailey**. I am going to do something I should not do, because I think most of you know my skepticism. What could I eyeball-in as a number of jobs? Are we talking about 300,000 jobs, half a million jobs? What are we talking about?

Mr. **Nehmer**. For both direct and indirect employment, our guess is, because we did a similar study——

Mr. **Bailey**. Could you do some work on that?

Mr. **Nehmer**. It would be about 350,000 jobs.

Mr. **Bailey**. About 350,000. That would square with your relationship of 2 to 1.

Mr. **Nehmer**. That is correct.

Mr. **Bailey**. OK.

Mr. **Miller**. If I may add something. What happens, since we are most severely depressed and penetrated, what happens to a manufacturer that has several suppliers in each area, as business begins to contract—in other words, people close up—the suppliers start either looking elsewhere and in most cases start closing up. So it is sort of a downhill thing that keeps on dragging you down.

Where we had five or six guys 4 or 5 years ago to call for basic things like vinyl and linings, they do not exist. Now there are two people around. So it keeps on going downhill.

I will give you a good example. Right now times are a little tough in retailing. Most of the imports have been bought on a letter of credit several months ago. When times get tough here, the first ones they cut off are the ones sitting at this table. The imports just keep on rolling in.

And then as the business gets bigger, what happens is there is a VP in Hong Kong and one in Florence who only has one thing to talk about—imports. His job, his salary, his incentive, depends upon how big a job he does over there. So there are a lot of other ancillary things that keep them going down. As you get to 75 percent import penetration, it gets more difficult to fight.

Mr. WEINER. This is particularly important because the kind of signal this policy sends to people in these industries is get out. The kind of signal you are talking about here is that the Government is not interested in seeing people stay in these industries.

Mr. BAILEY. What is your investment in plant and equipment? Do you know? Does anybody have a figure?

Mr. NEHMER. I am not sure if the Government has collected any data on this. But it does appear for the footwear industry because of the ITC investigations, and perhaps also on leather wearing apparel. I would like to have the opportunity to see what is out there in published data to provide it as far as capital investment is concerned.

Mr. BAILEY. OK. That would be an important figure to know.

[The information follows:]

The following tabulation provides new capital expenditures in the leather-related industries for 1978 and 1979, by specific industry group. The data are the latest official data available. Data on capital investment, per se, are not available. As can be seen, new capital expenditures from all leather-related industries were $76.6 million and $83.3 million in 1978 and 1979, respectively.

NEW CAPITAL EXPENDITURES IN THE LEATHER-RELATED INDUSTRIES FOR 1978 AND 1979

[In millions of dollars]

Industry	1978	1979
Nonrubber footwear	$40.7	$60.0
Gloves	10.2	2.9
Leather apparel	2.6	1.1
Luggage	9.3	11.1
Handbags	7.7	4.6
Personal leather goods	6.1	3.6
Total, leather-related industries	76.6	83.3

Source: U.S. Department of Commerce, 1979 Annual Survey of Manufactures.

Mr. BAILEY. I realize there is a vibrant, living, alive real estate market out there for these shops and factories, and I know people are going to be banging down your doors to buy them and put replacement industries in there. And I know it is going to be very difficult for you to resist the temptation to sell at two or three times what they are worth.

But this idea comes in with an add-on, 75 percent, 25 percent add-on. I do not know if you know anything about this, and it is probably not a reasonable question to ask, but is there any reason to assume you are going to get more than that 25 percent added on in order to take advantage of that duty-free market down there in Central America?

In other words, are we going to get Eastern products shipped in with a little bit of value added to them and then brought in here duty free? Are we going to see 50 and 75 and 100 percent of these items produced in those countries down there? Or do you think they are going to respond by raising barriers to those Eastern products?

Mr. NEHMER. If I may just comment on it, and perhaps my colleagues also have a comment. We have not commented in our oral discussion today, although we have in our written statements, about the 25-percent rule of origin local content level.

We find it incredible, very frankly, that the 35-percent level that appears under the GSP has been reduced to 25 percent. There is no question in my mind or the minds of my colleagues that it would be possible for——

Mr. BAILEY. Do they do that today?

Mr. NEHMER. To the Caribbean? Not that I am aware of in the Caribbean, no. But with the incentive provided with duty-free access to the United States, there is no question about it.

Let us just take the question of the canvas uppers that are used for shoes. They are excluded from duty-free treatment because they are made of textiles and therefore excluded. But if shoes become duty free on entry into the United States, we foresee canvas uppers coming into the Caribbean, assembled into shoes, the shoes come in duty free. And the 25-percent limitation is not going to stop this.

Mr. WEINER. There is an overcapacity in the Far East in our type of commodity, and I just cannot see that these people are going to do anything but protect their market by shipping as much product as they can into the United States. If they have to do it through the Caribbean, so be it.

Mr. GUNDERSHEIM. It seems to me what is being set up is a tremendous incentive to transship through the Caribbean. You can do 90 or 95 percent of a product, send it to the Caribbean, do some paper transactions, because you do the paper transactions—because the incentive of the duty free is more than enough to cover, to make up the difference and so on.

Mr. BAILEY. That is what I was going to ask.

Mr. GUNDERSHEIM. I think you are going to see a very substantial movement of products without any real benefit to the countries involved.

Mr. BAILEY. That is what intrigues me, the transshipment idea. I just have a hard time figuring that when it comes down to the value added that that 25 percent is going to represent that much labor done by poor folks in Central America. Of course, I do not know.

Mr. NEHMER. I would have thought the executive branch would have proposed an increase in the local content.

Mr. Bailey. Quite frankly, it is one of the anomalies. I do not know why. That is one that has got me stumped. I would have thought there would have been, if anything, some enforcement or some increase in local content requirement. And maybe they did not think of it, because I do not think this has been studied out very well.

I have got to tell you the truth: The testimony indicates it is very poorly analyzed.

Mr. Nehmer. We pointed out to you that they had not thought of the factor of safeguards. That test would not apply to footwear because they are using the escape clause, and footwear is not eligible to apply again under the escape clause until July 1, 1983.

Second, this Caribbean Basin Initiative in the legislation that has been put forward includes all the insular possessions of the United States. It is not limited to Caribbean insular possessions. It is very clear, the other ones—Guam, American Samoa—are covered by the duty-free provisions of this legislation as put forward by the administration.

Mr. Bailey. Do any of you represent any interests that work out of Puerto Rico or the Virgin Islands? Do you represent people down there?

Mr. Gundersheim. We have several thousand members in Puerto Rico between the two unions.

Mr. Bailey. Have you analyzed this thing in terms of its impact on Puerto Rico?

Mr. Gundersheim. Yes. To oversimplify, we think that Puerto Rico is going to be the overwhelming loser.

Mr. Bailey. I do, too.

Mr. Gundersheim. I was quite amazed to find representatives of Puerto Rico endorsing it wholeheartedly, at the same time enumerating all of the plants that have closed already. And it seems to me it has got to be in anticipation of further plant closings, for the simple reason that the wages in Puerto Rico are now at this point at the minimums required in the United States, and more than that actually.

The whole economic development of Puerto Rico has reached a point where production is comparable to the United States, and when you get 50 miles away, the Dominican Republic or Haiti, the wage level is probably one-tenth of what they are in Puerto Rico. I do not see how Puerto Rico can conceivably continue as a production base.

Mr. Bailey. I think there might be some indication that there is a desire to export those jobs, but avoid immigration problems, too. Which brings me to point number three. And thank God, Mr. Chairman, it is my last point. You have been very patient.

The people that are being replaced, the women—you do not have any statistics on how many of them are heads of households, I assume. Blacks, Hispanics.

Mr. Nehmer. Many came from the Caribbean in recent years to get jobs in these industries. They are the ones that have been the most recent entrants into the industry. So they are going to be the first out.

Mr. Bailey. In terms of the skill levels that they have and those kind of things, you know, what is going to happen to them. Of course, they are going to be thrown right out in the street. That is all that is going to happen to them. It is no more complicated than that.

I just get awfully angry at the numbers. It is only a few hundred thousand, that is all, just a few hundred thousand.

Mr. **Gundersheim**. It goes to more than that. It goes to your first point of basically what provision has been made to deal with that problem here domestically. And frankly, the labor movement gets a little angry about this because part of the covenant of the Trade Act of 1974 was that in return for an opening of the world markets through tariff reductions and other international negotiations and the benefits of free trade, that provision would be made for readjustment. There would be training for workers, provisions for technical help assistance to corporations to get into new lines of work, new industries, and so forth.

Well, the problem is they have gone ahead with all of the elements to open up trade but they have gone the opposite direction in terms of assistance and providing people with training opportunities and assistance in entering new lines of endeavor.

The Caribbean policy unfortunately goes even one step further. It gives positive incentives for corporations to go down there without any risk, frankly. They are given all the tax incentives and tax breaks. They are given special insurance to cover all their risks so that if there is a problem they do not end up as a loser. The only loser is the American worker who has nothing to fall back on because he is the one who is left with no insurance to cover his loss of income. What has he got?

Mr. **Nehmer**. The statement made by Ambassador Brock in his March 17 statement to this group on this question we are talking about has to be, I must say, one of the more misleading statements that has been made. He said: "We think that such an immediate extension of duty-free access on products that have not previously been included in the GSP scheme is warranted and does not pose a threat of injury to any affected U.S. industry." Remember, every one of these industries here with some very minor exceptions has been excluded from the GSP because of import sensitivity. Continuing to read from Ambassador Brook's remarks: "Should, however, a threat of injury or injury itself, actually develop, we will retain the ability to safeguard U.S. industry from Caribbean products using the same remedies available under sections 201 and 203 of the Trade Act of 1974"—when the record of the escape clause has been so dismal and these industries themselves have tried the escape clause and have had disastrous results.

Mr. **Bailey**. Mr. Chairman, was it the U.S. trade representative, who is asked to comment normally and they were excluded? Was it the trade commission, the ITC, who is asked to comment on the impact of those imports? Do you know they were specifically exluded from being contacted and asked to evalute the displacement in those kinds of things. Are you aware of that?

When the legislation was being written that specific was raised and they were specifically excluded.

Mr. **Nehmer**. I did not know that.

Mr. **Bailey**. I wanted you to know that as far as intentions go, it is something that frightens me. All right, State by State, where are these jobs located? Are they pretty much dispersed across the country? And last, let us say you had a totally duty-free environment going both ways; could you sell anything down there? How would you deal with that down there?

Mr. **Nehmer**. Each of these industries does have a certain amount of exports. The luggage industry has had for some time a certain amount of exports, and the footwear industry has increased its exports. I would say the areas we are talking about, however, as beneficiary countries are not of any significance for the exports of these products.

Mr. **Bailey**. How much do you export overseas? Do you export to these industries here?

Mr. **Weiner**. I think about 7 percent of the domestic shipments of luggage.

Mr. **Bailey**. That is going to dry up, too, is it not?

Mr. **Weiner**. The problem is also one of quotas. I think in the testimony from the shoe industry it mentions one of the governments of South America has a quota that you can bring in 12 pairs of shoes.

Mr. **Bailey**. That is Panama.

Mr. **Weiner**. That is typical of what is experienced. It is really significant that all these countries that have these types of industries have high tariffs. We mentioned 90 percent before. This is typical of what happens in these countries. Obviously, they are afraid of what would happen to their industries if they allowed free access to the markets.

Mr. **Bailey**. Well, I will tell you folks, I just want you to know that you have got a great deal of respect here being sacrificed on the altar of free enterprise. You should go smilingly to your economic demise. You owe it to your country to give up your livelihood and your standard of living. I do not think it is going to strike much of a blow for free enterprise. I really do not. If it did I would be for it.

Most of the members of the committee know where my views are regarding investment and savings and things like that. This is not going to do that much, it really will not.

Mr. **Nehmer**. I cannot believe the committee would report out a bill affecting an industry like this, which would represent such a major departure in trade policy and could do such harm to this segment of the American industry.

Mr. **Bailey**. If this policy succeeds as written, what you are going to see is a loping kind of improvement and help and you will be back 10 or 12 years from now saying oh, my God, we are dependent on a special arrangement, and we are going to have to increase this protection. Just one more hypocritical distortion of those kinds of allocations of resources that we are always screaming about in the international arena. That is all that it is. It is a mistake, I think.

I appreciate and thank you very much for the testimony.

Chairman **Gibbons**. Thank you.

Our next witnesses are Mr. Bobby McKown, who is the executive vice president of the Florida Citrus Mutual, and Mr. W. Amory Underhill. Gentlemen, both of you are certainly well-known to me. I welcome you to Washington and to this forum. And I previously received some other correspondence from you on the subject, but you may proceed as you wish.

STATEMENT OF BOBBY F. McKOWN, EXECUTIVE VICE PRESIDENT, AND GENERAL MANAGER, FLORIDA CITRUS MUTUAL

Mr. McKown. Thank you, Mr. Chairman. Mr. Bailey, members of the committee, it is our pleasure to be with you this afternoon, and we thank you for the opportunity to talk to you about important matters that impacts upon the Florida citrus industry.

My name is Bobby F. McKown. I am executive vice president and general manager of Florida Citrus Mutual. We are a voluntary cooperative trade association whose membership consists of 13,255 Florida citrus growers, and today my statement is concurred in by the State of Florida, the Department of Citrus and the Florida Citrus Packers Association as well. And a description of these organizations is attached to my brief.

Mr. Chairman, we understand the general thrust of the Caribbean Basin Initiative as developed and recommended by President Reagan and we further understand that the basin includes some two dozen small developing countries. Florida Citrus Mutual and the Florida citrus industry sincerely believe that certain assistance might be warranted for those specific countries. However, it is essential to this industry's well-being that certain safeguards be built into any plan which the Congress might approve.

Citrus has been judged to be import sensitive by the U.S. Government, International Trade Councils, and has continued to be reaffirmed by the U.S. International Trade Commission, the Kennedy Round, et cetera. The Florida citrus industry is the second largest industry in the State of Florida. We provide significant stability to our economy within the State of Florida.

I might point out to you that the largest citrus-producing county in the State of Florida, Polk County, producing about the same quantity of citrus that the entire rest of the United States produces at this time, currently has one of the highest unemployment rates in the United States, some 15 percent.

I point out that Florida's climate is similar to that of the countries in the CBI, and we believe that Florida and California could be adversely impacted more than other States because of our tropical agriculture, should fresh citrus and processed citrus products be allowed to enter under a reduced tariff or duty free. For every $1 of revenue lost in the production of citrus, the loss to Florida's economy would be $2.67, based on a multiplier developed by the University of Florida.

I might point out that Florida citrus growers have $8½ billion invested in the land and the trees, and that does not include plants or any other capital production equipment. Only in the trees and the land itself. We know that many of the CBI countries have serious problems with disease and insects, such as the Caribbean fruitfly, the Mexican and Mediterranean fruitfly, citrus canker, et cetera, which could be devastating to the Florida citrus industry, particularly if we have any greater exposure via expanded imports.

Increased imports coming into Florida and the United States from those countries would substantially increase our grower-members' risk of infestation by those insects and contracting some of those dreaded diseases. Florida Citrus Mutual respectfully requests that the Animal and Plant Health Inspection Service of the U.S. Department of Agriculture be invited to participate in the formulation of any possible implementation so that proper inspection safeguards would be included.

I might point out to you that additionally the Reagan administration now is proposing to reduce the number of inspections at small airports coming into Florida. We do not believe that is in the best interest of the Florida citrus grower in particular because you have many small planes coming in now, and last month at Port St. Lucie and Ft. Pierce they had 45 incidents where people had brought in diseased materials, and without that inspection program they would have entered the State of Florida undetected.

Any increase in shipments would mandate increased inspection at ports of entry, customs, and not less, as has been promoted by the administration's red door/green door policy. Adequate prevention is the best cure.

American farm income has continued to decline during the past 3 years, and 1982 does not offer any hope for turnaround in this regard. We believe that precautions must be taken to insure that these countries do not ship large quantities of fresh fruits and vegetables and citrus products into our domestic market, thereby disrupting our current marketing program. For every 1 million gallon increase in imports—that's juice—the total revenue for the Florida citrus industry would be reduced by 4 million at the wholesale level.

These countries do not have the stringent government regulations of the United States, the fruit maturity standards, the USDA grade standards for fresh and processed fruit, nor are they subject to the EPA pesticide limitations as are our growers. A primary concern we have is that these countries will be used for transshipments as a conduit for shipments to the United States duty free.

There is no need to offer this to them because we are now sharing our market duty-paid with other citrus-producing countries of the world which I will talk about in a moment.

Florida Citrus Mutual believes and advances its belief that the Congress should build in adequate safeguards to prevent these countries from being used as a conduit, as I said before. For example, Brazil or Surinam could circumvent the U.S. tariff by exporting through certain countries within the Caribbean Basin, thereby gaining reduced tariffs or duty-free access to our market. We suggest that at least a certificate of origin be required in order to negate this transshipment possibility.

If this loophole is not closed, then it would violate the intent and congressional purpose of the Tariff Act of 1930 as amended. Furthermore, it would severely adversely impact on our domestic market for fresh and processed citrus products which our industry has developed without Federal Government subsidy or tax benefits.

I might point out at this time that we are importing significant quantities of juice from Brazil, also from Belize and other countries duty paid, and it is not impacting adversely upon the consumer. In fact, in real terms, as I will cover a little later, our real term dollar value on an ounce-for-ounce basis of juice sold in the United States is less now than it was 10 years ago.

We also urgently request that any agreement the United States consummates with these countries should only be based on two-way trade. If we are going to open up our borders to them for citrus, they should be required to open their borders to us. This is and has not been true of most of our past trade agreements.

It is our understanding that certain products and goods are exempt from the proposed Caribbean Basin Initiative, and we respectfully request that fresh citrus and processed citrus products, both concentrated and nonconcentrated, sections and salads and essential oils be exempt, as they are very sensitive to import competition.

We strongly believe and respectfully request that the U.S. tariff schedules for all citrus and citrus products remain in place and be excepted from any bilateral or multilateral negotiations, treaty or other U.S. Government initiatives in order that we as an industry can continue our job of producing U.S. citrus and citrus products at a reasonable price for the consumer. The current tariff structure is performing and performing well.

For your information, the current tariff rate on citrus juices, not concentrated, is 20 cents per gallon. On concentrated it is 35 cents per equivalent gallon, single strength. Brazil and Mexico are the current largest suppliers; however, Belize and other smaller citrus-producing countries within the basin have also shipped limited quantities to the United States, tariff paid, without adverse impact upon them. I call to your attention that in 1978 we imported 148,099——

Mr. BAILEY. Mr. Chairman, I am going to run over and vote. I will not be able to return. I just want to tell the gentleman that I have gone over the statement, and as you can probably tell from my earlier remarks, I find myself very sensitive to many of your feelings.

Chairman GIBBONS. Let me say at this point we have eight votes that will take 40 to 45 minutes, and I think we had better recess at this time and I will come back at 4:30.

Mr. BAILEY. Mr. Chairman, I will not be able to come back, but then no one in the Congress could represent the interest of Florida better than the chairman.

Chairman GIBBONS. We will have to recess until 4:30. If I can come back earlier I will. I just do not know what is going to happen. I will be right back.

[Recess.]

Chairman GIBBONS. The meeting will continue.

Mr. McKown.

Mr. MCKOWN. OK. Mr. Chairman, to continue my remarks, Mr. Chairman, to point out how we are operating now under the current tariff system, we are importing juices duty-paid, and it is not having—these countries are sharing in our market and paying the duty, and it is not being disruptive to their program.

For instance, in 1978 in single-strength gallons alone we imported 148,000. That has increased to 10 million gallons in 1981, duty-paid. The value of those same imports in dollars has increased from $547,000 to over $15 million.

And in the area, again, we are operating with the import duty paid in the area of frozen concentrated orange juice, and that is the largest product we import. We have shown dramatic increases. For example, in 1981 there were 217.6 million gallons single-strength equivalent, as compared to 31.4 million in 1976, all tariff-paid.

These data vividly point out that imports duty-paid of orange juice and orange juice concentrate coming into the United States in large quantities are not being deterred by the U.S. tariff. Generally, we have imported all duty-paid and we see no reason to remove the tariff structures to these other countries.

More importantly, the tariff structures certainly cause no adverse economic impact on the U.S. consumer. Research indicates grapefruit juice prices in real terms have declined. Orange juice concentrate, chilled and canned, real-term prices have also declined relative to the price of all other consumer items. These real term price declines have occurred even though Florida encountered a number of severe freezes in 1977, 1980, 1981, and 1982.

For example, in 1972, 1971–72, the frozen concentrated orange juice price was $1.88 per dozen 6-ounce cans, and in real terms the 1980–81 price was only $1.79 per dozen 6-ounce cans.

We believe it is important to recognize that a large number of our processed products constitute a closely related group of citrus articles, all of which are essential food products for human consumption. This closely related group of processed citrus products is highly important to our industry and makes up a major segment of our citrus industry's products.

In fact, the Florida citrus industry, as you know, produces about 92 percent of all oranges going into processed citrus products. Frozen concentrated orange juice is being used more and more in other orange juice products because of the economics of transportation, technological advances, improved processing techniques, and improved distribution of our products in U.S. markets.

Any reduction in our current rate of duty, and certainly allowing duty free entry, would adversely impact upon the economic stability of our industry. A reduction in tariff or duty free or preferential treatment would further increase citrus supplies and destructively reduce citrus prices short-term. In the long term, lowered tariffs on citrus would result in curtailed Florida production because of unfavorable cost-price relationships, the ultimate outcome being reductions in citrus-related employment.

Currently, the average citrus prices are only 64 percent of parity in the case of grapefruit and 46 percent in the case of oranges. The long-term impact on the U.S. consumer, however, would be increased prices resulting from reduced Florida supply—an OJ OPEC.

We also know that no foreign supplier's quality control program equates to our continuous Federal-State inspection program which our industry has so strenuously followed in order to maintain and insure U.S. consumers' confidence in Florida citrus products. Therefore, the U.S. consumer, after gaining reduced prices for a short term, would subsequently endure higher prices for lower quality for a relatively long period.

Mr. Chairman, I point out it takes a long time--25 years—for a citrus tree to reach maximum production. Obviously, once a transition begins, an immediate reversal is not possible.

If you should go into the Central American countries and begin to plant citrus fruit trees, it would be 7 years before they would begin to reach commercial production and harvest any citrus fruit. It would take 25 years to obtain maturity production—a long-term investment. Once this begins, it would be hard to turn it back.

It should be pointed out that our industry is a free enterprise industry. It is an industry whose growers over the last 10 years have invested over $300 million of their own money to create and develop and expand our U.S. domestic and export markets, thereby contributing positively to our balance of payments.

Today we are fighting tariff barriers and value-added taxes in certain foreign countries which are deterrents to our growth opportunities abroad. We ask your consideration and assistance in this area, and point out that this situation should be borne in mind also in other negotiations.

Our industry is not price supported, nor Government subsidized. We are an industry that has developed its own marketing techniques and improved its own processing techniques, and an industry which has shared its technology with other citrus-producing countries, an industry which represents a strong base to the overall economy of our State as well as our country. We employ 86,000 people directly; indirectly, we create another 87,000 jobs within our State.

The Florida citrus industry and the U.S. citrus industry is labor intensive. That includes the production level in the groves all of the way through the distribution system.

The foreign supplier, including the basin countries, who wishes to move into this market in general enjoys a cost of production advantage due to lower wage rates and fewer governmental requirements to protect the consumer and the environment. Additionally, government subsidies for exports of many other citrus-producing countries are in many cases quite different.

I respectfully request that you particularly review one page of highlights reproduced and attached to our report "Mexican Producers Look to U.S. Market To Absorb Bigger Output." I quote the first paragraph. It says:

> Mexico's citrus industry, already largely dependent on the U.S. market for much of its export sales, is increasing production and is looking to the United States to absorb much of its expanded output, both fresh and processed.

It goes on to say they are increasing their plants from 6 to 15. I know that in Mexico—and we recognize that they are in part supporting the Caribbean Basin Initiative, but we have strong reason to believe that they too will petition for preferential treatment, because they have in the past.

We are currently sharing our market with these countries with duty paid. To ask us to share a market duty free which we have developed with Florida growers' money, with other citrus-producing countries whose competitive advantages far outstrip our ability to compete is asking and inviting a viable U.S. industry to compete at an unfair disadvantage. We believe that the magnitude of the

Caribbean proposal to reduce the tariff on Florida citrus fruits and products is very serious.

We have seen another country, Brazil, build an entire export industry based upon a Florida freeze. We have seen them build an industry that is now approaching the size of ours, yet an industry that utilizes none of its products for home consumption. By that I mean Brazilian frozen concentrated orange juice is not consumed in any quantity in Brazil.

In fact, they are producing almost as much processed citrus as we are in the United States. Their entire industry is built for export purposes, and it is built to move into our already grower-developed markets, competing with unfair competitive advantages which we have already presented. I might point out for the record that 98 percent of the total production in the country of Brazil is destined for export.

In summary, Florida citrus products are very sensitive to import competition at home and export competition abroad. Any reduction of the U.S. tariff would impact negatively on U.S. consumers, citrus processors, citrus packers and citrus growers. Safeguards must be put in place to prevent these countries from being used as a conduit for transshipment for others.

We strongly set forth that if any trade liberalization should be negotiated between this country and citrus producing countries of the Caribbean Basin Initiative, our Government should recognize and take into account those citrus items that are price sensitive and they should not be included in the final proposal.

We sincerely request that this subcommittee find, after reviewing our statement, that citrus fruit and citrus products should be excepted from any tariff reduction during the course of any international trade negotiations and development of the Caribbean Basin Initiative. We believe we have amply supplied sufficient justification with supporting data for this decision. In addition to my statement today, I plan to provide a more detailed brief for your full review.

I thank you, Mr. Chairman and members of the committee, for allowing Mutual an opportunity to be here today to present our statement in opposing any change in tariff rates for citrus. If you have need for any additional data, I stand ready to supply same.

[The prepared statement with attachments follows:]

STATEMENT OF BOBBY F. MCKOWN, EXECUTIVE VICE PRESIDENT AND GENERAL MANAGER, FLORIDA CITRUS MUTUAL

Good morning, Mr. Chairman and members of the subcommittee, my name is Bobby F. McKown. I am Executive Vice President and General Manager of Florida Citrus Mutual, a voluntary cooperative trade association whose membership consists of more than 13,255 active Florida citrus growers, with headquarters at Lakeland, Florida. The State of Florida, Department of Citrus and the Florida Citrus Packers support the position as set forth in this statement; a brief description of these organizations is attached.

We understand the general thrust of the Caribbean Basin Initiative as developed and recommended by President Reagan and we further understand that the basin includes some two dozen small developing nations in Central America, the Caribbean and northern South America. Florida Citrus Mutual and the Florida citrus industry sincerely believe that certain assistance might be warranted for those specific nations; however, it is essential to this industry's well-being that certain safeguards be built into any plan which the Congress approves. Citrus has been judged to be import sensitive by the U.S. Government, international trade councils, and it has continued to be reaffirmed by the U.S. International Trade Commission, Kennedy Round, etc.

Mr. Chairman and members of the Subcommittee, the Florida citrus industry is the second largest industry in the State of Florida and provides significant stability to its economy. Florida's climate is similar to that of the countries of the Caribbean Basin Initiative and we believe that Florida and California could be adversely impacted more than other states because of their tropical agriculture should fresh citrus and processed citrus products be allowed to enter under a reduced tariff or duty free. For every $1.00 in revenue lost in the production of citrus, the loss to Florida's economy would be $2.67 based on multiplier developed by the University of Florida.

We know that many of the Caribbean Basin Initiative countries have serious problems with disease and insects, such as Caribbean fruit fly, Mexican and Mediterranean fruit flies, citrus canker, etc. which could be devastating to the Florida citrus industry, particularly if we have any greater exposure via expanded imports. Increased shipments coming into Florida and the United States from those countries would substantially increase our grower members risk of infestation by those insects and/or contracting some of those dreaded diseases. Florida Citrus Mutual respectfully requests that the Animal and Plant Health Inspection Service of the U.S. Department of Agriculture be invited to participate in the formulation of any possible implementation so that proper inspection safeguards would be included. Any increase in shipments would mandate increased inspection at ports of entry, customs, etc. and not less, as has been promoted by the Administration's red door/green door policy. Adequate prevention is the best cure.

American farm income has continued to decline during the past three years and 1982 does not offer any hope for a turnaround in this regard. We believe that precautions must be taken to ensure that these countries do not ship large quantities of fresh citrus and processed citrus products into the U.S. domestic market, thereby disrupting our markets. For every one million gallon increase in imports, total revenue for the Florida citrus industry would be reduced by $4 million at the FOB level. These countries do not have the stringent government regulations of the U.S. fresh fruit maturity standards, USDA grade standards for fresh citrus and processed citrus products, nor are they subjected to the EPA pesticide limitations as are our growers.

Florida Citrus Mutual believes and advances its belief that the Congress should build in adequate safeguards to prevent these countries from being used as a conduit by some of their neighbors to the south and/or other parts of the citrus producing world. For example, Brazil or Surinam could circumvent the U.S. tariff by exporting through certain countries within the Caribbean Basin, thereby gaining reduced tariffs or duty-free access to U.S. markets. We suggest that a certificate of origin be required in order to negate this transshipment possibility. If this loophole is not closed, then it would violate the intent and congressional purpose of the Tariff Act of 1930 as amended; furthermore, it would severely adversely impact on our domestic market for fresh and processed citrus products which our industry has developed without federal government subsidy or tax benefits.

We also urgently request that any agreement the United States consummates with these countries should only be based on two-way trade. If we are going to open up our borders to them for citrus, they should be required to open their borders to us. This is and has not been true of most of our past trade agreements.

It is our understanding that certain products and goods are exempt from the proposed Caribbean Basin Initiative and we respectfully request that fresh citrus fruits, and processed citrus products (concentrated and not concentrated), sections and salads, essential oils be exempt as they are very sensitive to import competition.

We strongly believe and respectfully request that the U.S. tariff schedules for all citrus and citrus products remain in place and be excepted from any bilateral or multilateral negotiations, treaty or other U.S. government initiatives in order that we as an industry can continue our job of producing U.S. citrus and citrus products at a reasonable price for the consumer. The current tariff structure is performing and performing well.

The U.S. tariff rate on citrus juices, not concentrated is 20¢ per single strength gallon; frozen concentrated orange juice is 35¢ per equivalent single strength gallon, and these tariff rates have not prevented imports from coming into this country when needed, tariff paid. Brazil and Mexico are the largest suppliers; however, Belize and other smaller citrus producing countries within the basin have also shipped limited quantities into the U.S., tariff paid, without adverse impact upon them. I call your attention to the fact that imports under our citrus juices (not concentrated) tariff classification have increased substantially since 1977 as follows:

Gallons (single strength):	
1978	148,099
1979	221,796
1980	1,008,211
1981	10,096,688

The value of those same imports in dollars has increased from $547,081 in 1978 to over $15 million in 1981, according to U.S. Department of Commerce statistics.

Imports of frozen concentrated orange juice have also shown dramatic increases; for example: in 1981 there were 217.6 million gallons (single strength equivalent) as compared to 31.4 million gallons (single strength equivalent) in 1976, all tariff paid.

These data vividly point out that imports, duty paid, of orange juice and orange concentrate coming into the United States in large quantities are not being deterred by the U.S. tariff. More importantly, the tariff structure is certainly not causing any adverse economic impact upon the U.S. consumer. Research indicates that grapefruit juice prices in real terms have declined. Orange juice (concentrate, chilled and canned) real term prices have also declined relative to the price of all other consumer items. These real term price declines have occurred even though Florida encountered a number of severe freezes in 1977, 1980, 1981 and 1982. For example, in 1971-72 the frozen concentrated orange juice price was $1.88 per dozen 6 oz. cans, and in real terms the 1980-81 price was only $1.79 per dozen 6 oz. cans.

We believe it important to recognize that a large number of our processed products constitute a closely related group of citrus articles, all of which are essential food products for human consumption. This closely related group of processed citrus products is highly important to our industry and makes up a major segment of our citrus industry's products.

Frozen concentrated orange juice is being used more and more in other orange juice products because of economics of transportation, technological advances, improved processing techniques and improved distribution of our products in the U.S. markets.

Any reduction in our current rate of duty, and certainly allowing duty free, entry, would adversely impact upon the economic stability of our industry. A reduction in tariff or duty free or preferential treatment would further increase citrus supplies and destructively reduce citrus prices short term. In the long run, lowered tariffs on citrus would result in curtailed Florida production because of unfavorable cost-price relationships; the ultimate outcome being reductions in citrus related employment.

Currently, average citrus prices are only 64 percent of parity in the case of grapefruit; and 46 percent of parity for oranges, per the USDA September 1981 Agricultural Prices Report.

The long term impact on the U.S. consumer, however, would be increased prices resulting from reduced Florida supply—OJ OPEC.

We also know that no foreign suppliers quality control program equates to our continuous Federal-State inspection which our industry has so strenuously followed in order to maintain and insure U.S. consumers' confidence in Florida processed citrus products.

Therefore, the U.S. consumer, after gaining reduced prices for a short term period, would subsequently endure higher prices for lower quality for a relatively long period.

It takes a long time—25 years—for a citrus tree to reach maximum production. Obviously, once a transition begins, an immediate reversal is not possible.

It should be pointed out that our industry is a free enterprise industry. It is an industry whose growers over the last ten years have invested almost $300 million of their own money to create and develop and expand our U.S. domestic and export markets; thereby contributing positively to our balance of payments. Today, we are fighting tariff barriers and value-added taxes in certain foreign countries which are deterrents to our growth opportunities abroad. We ask your consideration and assistance in this area, and point out that this situation should be borne in mind, also.

Our industry is not price supported nor government subsidized. We are an industry that has developed its own marketing techniques and improved its own processing techniques; an industry which has shared its technology with other citrus producing countries; an industry which represents a strong base to the overall economy of our state as well as our country. We employ some 86,000 people directly. Indirectly, we create another 87,000 jobs within our state.

The foreign supplier, including the Basin countries, who wishes to move into this market that has been created by our growers, in general enjoys a cost of production advantage, due primarily to lower wage rates and fewer governmental requirements which protect the consumer and the environment. Additionally, government subsidies for exports of many other citrus producing countries are, in many cases, quite liberal.

I respectfully request that you particularly review one page of highlights (as reproduced from the FAS February, 1980 report) included in our brief regarding Mexican citrus producers. Particularly interesting is the headline of the story, and I quote: "Mexican Producers Look To U.S. Market To Absorb Bigger Output." I quote the first paragraph, "Mexico's citrus industry already largely dependent on the U.S. market for much of it export sales is increasing production and is looking to the United States to absorb much of its expanded output, both fresh and processed."

In another paragraph, and I quote: "Because of the belief that U.S. orange juice demand will remain strong and Mexican orange production will climb, Mexican orange producers are increasing the number of processing plants from existing nine, six of which produce juice concentrate, to 15 by 1981-82." The additional plants will in effect enable the industry to double its overall juice processing and evaporation capacity. Yes, we recognize that Mexico is supporting the Caribbean Basin Initiative, but we have strong reason to believe that they, too, will soon petition for preferential treatment.

To ask us to share a market, which we have developed with Florida growers' money, with other citrus producing countries whose competitive advantages far outstrip our ability to compete, is asking and inviting a viable U.S. industry to compete at an unfair disadvantage. We believe that the magnitude of the Caribbean proposal to reduce the tariff on Florida citrus fruit and citrus products is very serious.

We have seen another country, Brazil, build an entire export industry based upon a Florida freeze. We have seen them build an industry that is now approaching the size of ours, yet an industry that utilizes none of its products for home consumption. By that I mean Brazilian frozen concentrated orange juice is not consumed in any quantity in Brazil, and yet they are producing almost as much processed citrus as we are in the United States. Their entire industry is built for export purposes, and it is built to move into our already grower-developed markets, competing with unfair competitive advantages which we have already presented.

In summary, Florida citrus products are very sensitive to import competition at home and export competition abroad. Reduction of the U.S. tariff would impact negatively on U.S. consumers, citrus processors, citrus packers and citrus growers. Safeguards must be put in place to prevent these countries from being used as a conduit for others. We strongly set forth that if any trade liberalization should be negotiated between this country and citrus producing countries of the Caribbean Basin Initiative, our government should recognize and take into account those citrus items that are price sensitive and that they should not be included in the final proposal.

We sincerely request that this Subcommittee find, after reviewing our statement, that citrus fruit and citrus products should be excepted from any tariff reduction during the course of any international trade negotiations and development of the Caribbean Basin Initiative. We believe that we have amply supplied sufficient justification with supporting data for this decision. In addition to my statement today, I plan to provide a more detailed brief for your full review.

Thank you for allowing Mutual an opportunity to be here today to present our statement in opposing any change in tariff rates for citrus. If you have need for any additional data, we stand ready to supply same.

FLORIDA CITRUS MUTUAL, LAKELAND FLA.

Florida Citrus Mutual is now in its 32nd year as a Lakeland-based service and information entity for more than 13,255 citrus grower members banded together as a voluntary, private, nonprofit organization.

Its operations cover a broad spectrum of activities, all interrelated and with one purpose in mind—representation of the best interests of grower-members.

One of Mutual's main information services is daily market information upon which the grower can make his decisions concerning the marketing of his fruit. Along with market information, routine activities range from consumer demand studies, to efforts in seeing the development of the best possible advertising programs, improvement of quality of all citrus products, development of new products, maintenance of an adequate tariff structure, seeking standards of identify for citrus products, taking a direct hand in research and development of a workable mechanical harvesting system, achieving a theft and vandalism protection program and serving the growers' needs in such areas as pollution, taxation, water management, property rights, and also supporting with grower funds development of new markets for citrus products.

Basically, Florida Citrus Mutual deals in all those forces brought into play in production, distribution and marketing of citrus and citrus products.

Florida Citrus Mutual is governed by a 21-member Board of Directors elected annually by the membership.

FLORIDA DEPARTMENT OF CITRUS, LAKELAND, FLA.

The Florida Department of Citrus, formerly known as the Florida Citrus Commission, is a full-fledged department of the Executive Branch of State Government. It was established in 1935 to protect the health and welfare and to stabilize and protect the Florida citrus industry. It is headed by a board of twelve growers appointed to staggered 3-year terms by the Governor and confirmed by the State Senate. The board is known as the Florida Citrus Commission.

The Department is charged with the administration of the State Citrus Fruit Laws and under those laws it has broad regulatory and police powers with respect to packing, processing, labeling, and quality standards, etc., of Florida citrus fruit and products, and the licensing of those who deal with them. Also, the Department conducts extensive advertising and promotion programs and carries on continuing broad-scale scientific, economic, and marketing research activities, all in behalf of the Florida citrus industry. Current annual expenditures are approximately $32,000,000 funded exclusively from special excise taxes assessed on each box of citrus grown in the State of Florida.

A primary concern of the Department is the protection and enhancement of the quality and reputation of Florida citrus fruit and products.

Dr. W. Bernard Lester, Executive Director, Florida Department of Citrus, Post Office Box 148, Lakeland, Fla. 33802.

FLORIDA CITRUS PACKERS, LAKELAND, FLA.

Florida Citrus Packers is an organization representing 86 fresh fruit packers and shippers who account for over 90 percent of all fresh citrus shipped out of Florida annually, to domestic and export markets.

Florida Citrus Packers was formed to promote, foster and encourage the business of marketing fresh Florida citrus and to assist in addressing—cooperatively and collectively—the common problems of its members, including, but not limited to:

Marketing, research, quality regulation, transportation, legislative matters involving the citrus industry, insurance, labor, etc.

Mr. James E. Emerson, Executive Vice President, Florida Citrus Packers, Post Office Box 1113, Lakeland, Fla. 33802.

MEXICAN CITRUS PRODUCERS LOOK TO U.S. MARKET TO ABSORB BIGGER OUTPUT

(By John H. Wilson, Foreign Agriculture/February 1980)

Mexico's citrus industry—already largely dependent on the U.S. market for much of its export sales—is increasing production and is looking to the United States to absorb much of this expanded output, both fresh and processed.

Mexican orange juice producers believe that growing consumer demand in the United States for juice will permit Mexico to supply a larger share of the U.S. market.

Mexico's exports of fresh oranges and tangerines to the United States in 1978/79 were considerably larger than in the previous year, despite the drought in 1977 and severe freezes in December 1978 that lowered production.

The drought affected all of Mexico's producing regions but was most damaging in the States of Nuevo Leon, Tamaulipas, and San Luis Potosi. The freeze was primarily concentrated in the Montemorelos-Linares citrus region of Nuevo Leon, and caused output in this area to fall from the 1977/78 level by one-third. The three drought-affected States, plus Veracruz and Tabasco in the south, and Colima and Michoacan—Mexico's major lime producing States—account for the bulk of Mexico's citrus production.

Mexico's lastest official production figures are for 1977 and show citrus production of about 2.48 million metric tons: 1.86 million tons of oranges, 58,200 tons of tangerines, 112,100 tons of grapefruit, and 444,640 tons of limes.

Trade sources agree with these Secretaria de Agricultura figures, except they believe tangerine production was in the 125,000–130,000-ton range.

Despite the damage done by the drought, orange and tangerine output is expected to rebound sharply. By the mid-1980's, orange production is seen approaching 2.7

million tons and that of tangerines, 175,000 tons, largely because many new trees are beginning to bear and cultural practices have been improved.

New plantings, mainly of Valencia oranges and Dancy tangerines, were high in 1977/78 and 1978/79, encompassing areas from the southern tip of Tamaulipas State to the southwest coastal regions of the Yucatan Peninsula. Apparently, there is little room for expansion in traditional citrus area in Nuevo Leon.

Grapefruit and lime trees were least affected by the adverse weather because of their southerly location. About three-fourths of the grapefruit trees are in Veracruz and Tabasco, and the bulk of the lime trees are in Colima and Michoacan.

The rate of grapefruit tree plantings has been high since the early 1970's and production is expected to rise 50 percent from 1977 levels to about 170,000-175,000 tons by 1985. However, some industry sources have indicated that grapefruit tree plantings may be reduced substantially next season because of producer fear that a worldwide glut and a lessening of demand in the domestic market will cause market prices to fall.

A common concern among Mexican producers is the huge expansion of grapefruit plantings in Cuba. While the United States banned all imports from Cuba in 1962, Mexico is fearful that—if the ban is lifted—it may lose a share of the U.S. market.

Mexican lime production has stabilized during the past few years. The crop is divided between Key lime varieties (95 percent of output) and Persian varieties (5 percent).

All Mexican fresh citrus fruit exports pass through packing houses, of which there are 31. Twenty-six of these are located in Nuevo Leon and are members of the Mexican Association of Citrus Packers. The organization was established in 1964 to promote citrus production in Mexico and to improve quality and marketing opportunities for its members.

The fresh export market takes 1-3 percent of the country's oranges, 20-25 percent of its tangerines, 10-15 percent of its grapefruit, and about 1 percent of its limes. About 60 percent of Mexico's orange exports go to the United States and all of its tangerine shipments are to the United States and Canada.

Tangerine shipments are more or less limited to these countries because the fruit is susceptible to decay and peel injury brought on by excessive handling.

U.S. imports of fresh Mexican oranges and tangerines in the 1978/79 season (November-October) amounted to 46,096 metric tons—48 percent of the total were tangerines and 52 percent were oranges. This is a 70-percent gain over imports in the previous season.

Largely responsible for this increase were the short 1978/79 citrus crops in California and Arizona. Mexican shipments to the United States, especially of oranges, fluctuate considerably from year to year, mainly because of changes in U.S. demand and to a lesser degree because of shortfalls in Mexican production owing to frosts or droughts in Mexico's most important growing areas.

After the United States, the German Democratic Republic (GDR) is Mexico's most important orange export market. Latest official Mexican trade data (1977) show orange exports to the United States and the GDR were about evenly split at some 17,000 tons each.

Small amounts of oranges also go to the Netherlands. Mexican exporters normally ship as much fruit to the United States and Canada as they can and the balance to Europe, a market they are especially interested in enlarging.

Mexico's fresh grapefruit exports have doubled in the past few years, with the major markets being the United States, Western Europe (primarily the Netherlands and France), and, most recently, Japan. Shipments to Japan climbed from 90 tons in 1971 to 3,200 tons in 1978, exceeding the calendar 1978 U.S. import level of 1,260 tons.

Because of the early harvest in Veracruz, Mexican grapefruit hits the U.S. market 2-3 weeks before the U.S. shipping season gets underway. This gives Mexico a competitive advantage in some of its foreign markets.

Mexico hopes that, despite the anticipated larger world supplies of grapefruit, it will be able to keep its present share of the U.S. and West European markets, and increase its exports to Japan in the early part of the marketing year.

U.S. imports of Mexican limes have trended upward from 3,080 tons in 1974 to a record 12,330 in 1978. The increase is attributed to larger Mexican supplies of Persian variety limes, coupled with a drop in U.S. output, which fell from about 40,000 tons in 1974/75 (April 1-March 31) to 19,000 tons in 1978/79.

U.S. lime imports from Mexico continued at a relatively high level in the first 11 months of calendar 1979 (11,642 tons compared with 10,351 tons during the same period in 1978).

Because of a belief that U.S. orange juice demand will remain strong and Mexican orange production will climb, Mexican orange juice processors are increasing the number of processing plants from the extisting nine—six of which produce juice concentrate—to 15 by 1981/82. Three of the new plants will be located in Veracruz and one each in Nuevo Leon, Tamaulipas, and Yucatan.

The additional plants will, in effect, enable the industry to double its overall juice processing and evaporating capacity. The nine existing plants have the capacity to remove 131,000 pounds of water per hour and have a total of 60 extractors.

To imporve its competitive position in relation to U.S. and Brazilian orange juice, one of the largest existing Mexican plants at Montemorelos recently installed eight 100,000-gallon cold storage tanks to reduce its juice handling costs, insure uniform blend consistency, and facilitate bulk transfer. Similar tanks have been in existence in Florida for 5 years, but these are the first in Mexico.

By the middle of next season, this plant will begin to ship some of its output to the United States in bulk rather than in conventional 55-gallon drums, Frozen-slush juice will be transported by truck in stainless steel tanks holding 20–22 tons at temperatures below freezing.

The juice will be reconstituted and/or packaged in a nearby U.S. state. By shipping such large quantities of juice for the short distances involved, processors will realize a savings in fuel and handling costs.

About 70 percent of Mexico's orange juice output is exported. The United States takes about half of Mexico's juice exports, Canada, Sweden, the Bahamas, and West Germany are other important buyers.

U.S. demand for imported orange juice has been particularly strong in the past few years because the Florida freeze of 1977 pushed up prices for domestic juice. However, Mexico was unable to take full advantage of the market possibilities, largely because of a lack of processing capacity.

U.S. orange juice imports have soared from 31.4 million gallons (single-strength equivalent) in calendar 1976 to 150.7 million gallons in 1978. Almost all of the increase came from Brazil, which, as the world's No. 1 orange juice exporter, has capacity to produce 10–12 times more juice than Mexico. In 1978, U.S. imports of juice from Mexico amounted to 9.9 million gallons and those from Brazil, 139.5 millon gallons. During the first 11 months of 1979, Mexico shipped 7.2 million gallons to the United States; Brazil sent 134.4 million.

The Mexican orange juice industry is optimistic that U.S. demand will continue strong during the next several years, despite occasional fluctuations. It believes that U.S. population growth and the downward trend in Florida's orange-bearing area—which dropped from 660,000 acres in 1970/71 to 579,000 in 1977/78—will leave ample room for expansion of Mexican juice shipments.

There are four plants in Mexico that section citrus and other fruits and a fifth one is to be built by 1980/81 in Nuevo Leon. About 90 percent of Mexico's output comes to the United States and about 10 percent is shipped to Canada.

In calendar 1978, the United States imported 4,530 tons of Mexican prepared and/or preserved oranges and grapefruit (including citrus sections) valued at $2.2 million, and 4,040 tons of prepared fruit mixtures, worth $2.3 million. Fruit mixtures include several fruits in addition to citrus, such as apples, bananas, melons, and pineapples.

Reportedly, in 1978/79 the Mexican industry has been operating at close to capacity, largely because of the strong U.S. demand for sectioned fruit. But, since Florida's production has been declining in recent years, the new Mexican plant is expected to make more sectioned fruit (canned and chilled) available for export to the United States.

Florida accounts for about 90 percent of all U.S. sectioned fruit production. Since the mid-1960's, Florida's output has fallen by slightly over 50 percent and in 1978/79 it consisted of 5,950 tons of sectioned grapefruit, 2,400 tons of orange sections, and 8,700 tons of fruit salad.

U.S. fruit sectioners, already having difficulty competing with the Mexicans in terms of quality and production costs, may continue to have problems. The Mexican industry has available a large, low-paid labor pool, which enables the industry to produce hand-sectioned fruit. The U.S. product is sectioned by machine.

Mexico also is the world's leading producer of lime oil and juice and its oil exports take care of about 60 percent of global export requirements. Roughly three-fourths of Mexico's lime oil is exported and two-thirds of U.S. requirements come from Mexico. The United Kingdom also takes a sizable volume of Mexico's lime oil.

Most of Mexico's lime juice exports are in concentrated form. Two-thirds go to the United Kingdom, and about one-third is shipped to the United States. This country took 390,000 gallons (single-strength equivalent) of Mexican concentrated lime juice in 1978.

Since Mexico's lime production has stabilized, no significant near-term expansion is anticipated in the export of lime products. It is also likely the United States and the United Kingdom will continue to be Mexico's leading markets for lime oil and juices.

Chairman Gibbons. I thank you for your fine statement and for your patience in waiting while we had all of those votes, and your patience in waiting all day to be heard.

I understand your deep concern for the infestation of disease from the Caribbean and Central American countries and from other countries, and I hope our Government will make every effort to make sure that this does not happen.

Let me see. The main competitors to Florida now are, of course, Brazil with its very high production and very low domestic consumption, and Mexico is coming on strong with its very high production and very low domestic consumption. And then there is some in Belize, is that right?

Mr. McKown. That is right.

Chairman Gibbons. Are any other of the Basin countries producing citrus products?

Mr. McKown. Honduras has a small production, Mr. Chairman. Also, Costa Rica has about a 6,000 acre planting going in now, guaranteed by our Government through the State Department, as I understand it, and insured.

But by and large, the Caribbean Basin itself is not a large citrus producing area at this time.

Chairman Gibbons. So your main concern at this time really is disease and the Mexican threat if they petition for a reduction, kind of piggybacking upon what the Basin has.

Did you say in Costa Rica there is a 6,000 acre planning going on?

Mr. McKown. Yes, sir, a planned planting of 6,000 acres is under planning in Costa Rica.

Chairman Gibbons. What are these, oranges, grapefruits?

Mr. McKown. Oranges. I also have reason to believe they plan to develop a concentrate plant, a bulk operation, and export bulk juice in 6 to 7 years when those trees reach maturity.

Mr. Chairman, our other concern, our primary concern aside from the disease is the fact that they might be used as a conduit by Brazil and other citrus producing countries.

Chairman Gibbons. Yes, yes. I see that problem. Essentially, what you are afraid they could do is, you are afraid they could take a concentrate and repack it as fresh juice, as some Brazilian juice is now done.

Mr. McKown. Yes, sir.

Chairman Gibbons. I would not imagine that would get beyond the 25 percent value added requirement. They would not be doing anything except letting it thaw out and putting water in it, would they?

Mr. McKown. First of all, they could go into a reprocessing operation and put it into packaged case goods and be ready to ship in duty free and thereby go ahead and package it there. And that is not a labor-intensive element, whereas when you bring in the fresh fruit from the field all the way to the plants and process it, that is where you get your labor intensity.

Chairman GIBBONS. Still, I do not know that much about the economics of citrus. Under this proposal they would have to have a 25 percent value added?

Mr. McKOWN. Yes, sir, that is correct.

Chairman GIBBONS. And it is just my offhand guess—I have never studied it, but taking it out of a frozen container and putting it into another, reconstituting it, would not add 25 percent to the value. Have you all done any economic studies on that?

Mr. McKOWN. Yes. If they took it from 65 degree brix, a high concentrate, and then repackaged it into single strength juice at 11.8 degrees into a package ready to drink in the case goods, they would enhance the value by 25 percent by doing this.

Chairman GIBBONS. Just by adding water and putting it into a smaller container?

Mr. McKOWN. Yes, sir, and packaging it ready to go to the market, yes, sir. You see, the 65 percent is a concentrated 65-degree Brix. You take that and you would cut—manufacturer—that back to 11.8. So for every gallon on that basis, you would make 6.9 gallons of single strength equivalent, and you repackage that and thereby your carton and your labor and the glass bottle or whatever would add, I believe, 25-percent to that value.

But I would be glad to do some further checking.

Chairman GIBBONS. I would like to examine that further with you, because I do not think they ought to be able to take Brazilian juice and put water in it and in effect say they have added value to it. In fact, I would think they would have decreased the value of the juice, of the concentrate.

I see the problem. You are saying that they would take concentrated juice, dilute it, and because the diluted juice has a higher retail value and they would have to put it in a smaller package that would add 25 percent to the value of the juice.

Mr. McKOWN. Yes, sir. The finished product would have a 25-percent increase.

Chairman GIBBONS. I think that is something we must be concerned about. I am concerned about it. I do not see where that would be really doing anything for the Caribbean Basin. It would surely be doing a heck of a lot for the Brazilians, though.

Mr. McKOWN. Right, exactly.

Chairman GIBBONS. All right, sir. Thank you very much. We appreciate that very fine testimony.

Mr. McKOWN. Thank you, sir.

Mr. UNDERHILL. Thank you.

Chairman GIBBONS. Our next witness is a panel of members from the Virgin Islands. We have Mr. Williams, who is the chairman of the Committee on Commerce of the Legislature of the Virgin Islands; Mr. Lawaetz, who is the chairman of the Committee on Agriculture for the Legislature of the Virgin Islands; Mr. James Southerland, who is the president of the St. Croix Chamber of Commerce; and Margaret Creque, who is the first vice president and President-Elect of the St. Thomas-St. John Chamber of Commerce.

We are glad to have you here, and I apologize to you, lady and gentlemen, for keeping you so long today. But we wanted to have your testimony and to try to find out more about the problems as you see them from the Virgin Islands.

As you have perhaps heard from the statements that have been made today, there is on the part of committee members a very serious concern about what this does to a part of the United States of America that happens to be the Virgin Islands. Your Governor and your representative here in Congress have done an excellent job, and it has always been a pleasure to work with them, and we look forward to working with you.

Now let us see. Mr. Williams, you come first on the list, so we will hear you first.

STATEMENT OF HON. LLOYD L. WILLIAMS, CHAIRMAN, COMMITTEE ON COMMERCE, LEGISLATURE OF THE VIRGIN ISLANDS

Mr. **Williams**. Mr. Chairman, I would like to thank you very much for affording us the opportunity to address a very critical area, the Caribbean Basin Initiative for the Virgin Islands.

You have our written testimony before you and I would like to, because of the time——

Chairman **Gibbons**. All right, sir. We will put the statements of each of you in the record and you may summarize as you wish.

Mr. **Williams**. Yes, I will proceed to summarize.

Mr. Chairman, my name is Lloyd L. Williams. I am a senator, now in my fifth term, in the Virgin Islands Legislature, where I serve as chairman of the Standing Committee on Commerce. I am also the founder and past president of the West Indian Solidarity Committee in the Virgin Islands, and in that regard I am certainly happy about the administration's ideas about Caribbean development.

Most Caribbean countries have a number of significant problems in common, such as high rates of inflation, rapidly expanding youthful populations, growing unemployment, and general underdevelopment. The consequent political volatility of the region is a condition the United States cannot afford to ignore.

I am a servant of the proud people of the Virgin Islands, so I am truly appreciative of the opportunity to appear before the subcommittee. I realize the very difficult task you have ahead of you in considering this legislation and in coming up with what will be best for the country as a whole, for the Caribbean countries, and for the territories as well.

I feel sure that you too must be able to empathize with my situation in the Virgin Islands and with my responsibilities to the people of the Virgin Islands. Self-reliance for the Virgin Islands within the greater social, economic and political framework of the United States and the Caribbean Basin Initiative is a very attainable goal.

Virgin Islanders are loyal Americans. We have proved our loyalty continually during our 65-year relationship with the United States, which began in 1917 when President Wilson purchased our islands from Denmark. Our men volunteered to fight in World War II even though they were not required to do so. Virgin Islanders have always held loyalty to be an honorable and admirable trait.

We should not be hurt by the Caribbean Basin Initiative because we are loyal. We already represent the United States and the promise of America and democracy to many, many West Indians and West Indian countries.

Our population includes citizens from nearly every island who have come to the Virgin Islands for a chance in life. We must be allowed, in fact we should be encouraged, to develop self-reliance and to reduce our present economic dependence on the United States.

We are all aware of the regularity with which the Virgin Islanders come to Washington hat in hand for giveaways from past administrations and now from the current administration and Congress. We believe, however, that the heart and soul of the Reagan administration's policies, as well as of this distinguished subcommittee, is to promote self-reliance in the interest of good fiscal management and economic development.

However, we will need special assistance for this to develop in a positive manner which will reflect well upon the United States. Within the context of the Caribbean Basin Initiative, however, we will need more favorable treatment than the beneficiary countries in order to succeed in the Caribbean and to continue to grow in stature as a symbol of what the United States and free trade among countries can do in a unified Caribbean.

In my opinion, Mr. Chairman, the bill before you will have the effect of taking away our competitive edge. This makes the Virgin Islands more likely to become too dependent upon the largesse of the United States. The current bill establishing the Caribbean Basin Initiative Recovery Act would spell disaster for our economy if passed in its present form.

It would shake the economic foundations of our community and create economic instability in a U.S. possession. This instability could lead eventually to social and political unrest. It could also shake the faith that Virgin Islanders have in America and in the American system.

As it stands, the CBI is designed to include trade, aid and investment, to stimulate the private sector. The overall objective of CBI is to expand the productive sector to enable nations to increase their resource base, provide employment, and move toward economic self-sufficiency. If this policy is adopted as it is drafted, it will have the opposite impact on a U.S. possession.

The thrust is all toward foreign countries. The investment benefits being extended to the other Caribbean countries are undercutting our heretofore privileged position in having an ability to lure investment. Trade is being set up under this bill to favor the other Caribbean countries because when the Virgin Islands is only being kept on a par with tax and free trade benefits to beneficiary countries, the Virgin Islands is in fact below par in its ability to compete in the Caribbean marketplace.

As you will see, we have a number of major problems with this legislation as it is presently conceived. The problems, briefly stated, are as follows:

One, section 102, subsection (d), proposes to amend headnote 3(a) by adding "articles imported from insular possessions of the United States to receive duty treatment no less favorable than the treatment afforded such articles when they are imported from a beneficiary country under such Act." Because the beneficiary countries all have the cheap labor, lack of Federal regulations, and just as pleasant an environment to live in as we, the major problem with this provision is that being on par with these beneficiary countries will make it impossible for us to compete favorably.

Two, another problem we face deals with section 103, eligible articles. We have no raw materials to add as part of the 25 percent Caribbean value added being proposed. Further, we have no ability to compete for labor intensive processing because the other islands have a much cheaper labor pool to use.

Three, the "snap-back" provision, subsection D(2), does not hold any real protection for the Virgin Islands, though we are considered domestic for the purposes of this subsection, which does allow for the Virgin Islands to be eligible for import relief if there is serious injury to a domestic industry substantially caused by imports of articles receiving duty-free treatment under this title.

The problem with this provision is simple. Except for watches and rum, we might have no serious injury possible in the sense of this subsection. The serious injury will come to the Virgin Islands in a different form, that of not being able to attract or establish industries in the Virgin Islands at all.

The "snap-back" provision does not offer any safeguard for that; therefore, it is not going to provide adequate protection for the Virgin Islands in the area in need of protection.

Four, section 201, emergency economic assistance, excludes the Virgin Islands entirely. We will get neither oil nor foreign assistance from these other donor countries, and yet the Caribbean countries around us will get both oil and foreign assistance as well as economic assistance from the United States and other benefits through this legislation, which puts them on a more favorable basis than the Virgin Islands.

Five, investment tax credit and accelerated cost recovery, are nothing new for the Virgin Islands. Under our tax system, which reflects the same rules and regulations as the Federal system, we already have them. All this section does is further erode our advantages over other Caribbean countries, giving us nearly nothing in return.

Oil refining, tourism, rum, these are the foundations of the Virgin Islands economy.

First, Hess Oil Virgin Islands Corp. is the major industrial contributor to the Virgin Islands treasury. It has recently filed its corporate income taxes for 1981. The corporation shows substantial losses and will carry them forward, so we cannot predict with any accuracy what revenues, if any, we can expect from Hess in the near future as far as corporate income taxes are concerned.

Given the world oil glut which now exists and the fact that Hess Oil Virgin Islands Corp. has substantial losses, the government of the Virgin Islands faces the distinct possibility of not receiving corporate income taxes from its biggest taxpayer for the predictable future.

Second, with regard to tourism, the beneficiary countries all have the same Sun, sand, and sea. Tourism in the Virgin Islands is experiencing difficulty even with vigorous promotion. To some extent this is probably due to the recessionary trends in the States, which accounts for the lion's share of our tourism trade.

This is beyond our control, but another area hurting tourism is our decreasing competitiveness as a shopping port for tourists. The tourism reputation of St. Thomas and the Virgin Islands generally has always been that of a free port with bargains and prices better than other places. The price advantages were due primarily to the fact that tariffs on a large variety of items were considerably lower in the Virgin Islands than they were in the United States.

Over the past 20 years, tariffs on many of these items to the United States have either been eliminated or reduced very substantially. Thus, the competitive advantage enjoyed by the Virgin Islands has been lost on a number of items, such as electronics, camera equipment. Merchants in the Virgin Islands are no longer able to compete with prices available in the United States or in surrounding competitive markets.

Rum is one of our oldest and most reliable industries. Its importance is also critical to our economy. As Governor Juan Luis stated earlier, the excise tax which is returned to us each year on rum imported into the United States amounts to $37.1 million, or 15 percent of the Virgin Islands' budget. That money is earned through our own local rum production.

Frankly, Mr. Chairman, I am concerned about receiving the excise taxes on rum produced by other countries, as is proposed by the legislation before this subcommittee. That is revenue which we did not earn. It is in essence another handout and will only foster dependence.

The entire CBI holds the distinct possibility of fostering a dependency of the U.S. possession while bolstering the economies of the beneficiary countries so that they can benefit and become self-sufficient. Ten years from now, 12 years from now, another David Stockman may come along and ask why the Virgin Islands received excise taxes on other countries' rum and may want to cut out that kind of rebate to the Virgin Islands when he finds out that the Virgin Islands has no legitimate claim on that money.

We do have a right to the excise taxes we get on rum which we produce in the Virgin Islands. However, it seems to me that a proper approach would be to exempt rum from the free trade area completely. That is the only way to safeguard and guarantee our rum industry's potential for growth. If total exemption of rum is not desired by this subcommittee, at least set the policy in such a manner as to foster growth in the industry, not stagnation and possible loss of the industry.

A meaningful quota system might be an answer to gradual industry adjustment for the Virgin Islands. For example, rum might remain exempt on the free trade area for the first 5-year period. Then a gradually increasing system of quotas on duty-free foreign rum imports could be instituted. This would give the Virgin Islands the opportunity to make the adjustments necessary for a time when rum from other Caribbean countries may become more competitive.

There are possible solutions as well to other problems we have with the Caribbean Economic Recovery Act. After all, American policies were instrumental in developing our economy, especially the tourist shopping market. Congressman de Lugo has introduced bill No. 5113, which would reduce to 10 percent from 30 percent the tax rate on dividends, interest and other passive income flowing from the Virgin Islands to the United States and which would remove foreign tax credit restrictions as they relate to this tax.

H.R. 5113 was introduced by our V.I. delegate, Ron de Lugo. Section 103, eligible articles, can be amended to require that Caribbean goods pass through the Virgin Islands as a part of the value added formula. For example, if goods are shipped directly from a beneficiary country to the customs territory of the U.S., then the goods would be, say, 75 percent duty free. If the same goods came through the Virgin Islands, for example, the goods would gain the additional 25 percent duty exemptions so that the goods enter the United States 100 percent duty free.

The "snap-back" provision must reflect our lack of natural resources and our needs before it can do us any good. It must somehow safeguard industrial development in the Virgin Islands as an entity, not just individual industries which are in trouble because of the basin initiative.

There is no protection for businesses not locating in the Virgin Islands because of benefits to beneficiary countries. The snap-back concept must be broadened to include an injured State or territory.

We note with some chagrin the Virgin Islands is excluded from the $350 million appropriation for emergency economic assistance. Well, that is okay with me personally as long as we get some compensatory program to do for us at least what is being done for the non-U.S. areas.

There is another way of funding low-interest development loans and capital improvements and for rebuilding infrastructure with earned dollars, not giveaways. The source of funds is gasoline excise taxes on a product manufactured in the Virgin Islands. That is money, Mr. Chairman, that we have earned, and we desperately need such additional sources of revenue in order to adjust and move our economy in a self-sustaining and positive, growth-oriented direction.

The Small Business Administration, Economic Development Administration, and the Farmers Home Administration are being cut back to such an extent that there is little funding available for infrastructure improvement. Such improvement is needed desperately if we are ever going to get industry to establish in the Virgin Islands ports, water and power, and more specialized and sophisticated systems of accounting are needed. Yet, we are unable to get assistance from sources outside of the U.S. Federal programs.

Also, companies and industries wishing to invest in the Virgin Islands are unable to obtain low-interest loans from the World Bank, Inter-American Development Bank, International Monetary Fund, International Bank for Reconstruction and Development, and other international financial institutions.

Congress must remember that the Virgin Islands will not survive as a stable political entity and territory of the United States of America if you do not assist us in every way possible to keep our competitive edge. Our success can only serve to enhance the credit of the United States of America.

Mr. Chairman, my remarks are in the spirit of cooperation. They are meant to be informative in nature so that you may have the direct input of Virgin Islanders as you consider the Reagan administration's Caribbean Basin Economic Recovery Act. The urgency of the situation in the Caribbean demands action.

The right action must be an action or series of actions and policies which lead to helping all of us in the Caribbean and which provide continuing special assistance components for the Virgin Islands in order that we may grow and develop into the zenith of free enterprise, free trade, and democracy in the Caribbean.

What better result could come from a Caribbean Basin Initiative than to have such a bastion, such an outpost of free enterprise and democracy as the leader of the economically unified West Indies. The economic well-being of the Virgin Islands is in your hands. The fate of the Caribbean is in your hands. It is a grave and burdensome responsibility.

We are willing to do whatever we can to shoulder some of that burden with you, but we must be in shape to do so. We must become self-sustaining economically. The potential for that growth also rests in your hands.

That ends the testimony that I have to offer this afternoon. I thank you for your patience, Mr. Chairman.

[The prepared statement follows:]

STATEMENT OF HON. LLOYD L. WILLIAMS, SENATOR, FOURTEENTH LEGISLATURE, U.S. VIRGIN ISLANDS

Mr. Chairman, Members ot this distinguished subcommittee. My name is Lloyd L. Williams. I am a Senator, now in my fifth term in the Virgin Islands Legislature where I serve as chairman of the standing committee on commerce. I am also the founder and past president of the West Indian Solidarity Committee in the Virgin Islands. In that regard, I am certainly happy about the administration's ideas about Caribbean unity. Most Caribbean countries have a number of significant problems in common such as high rates of inflation, rapidly expanding young populations, growing unemployment, and general underdevelopment. The consequent political volatility of the region is a condition the United States cannot afford to ignore. I am a servant of the proud people of the Virgin Islands, so I truly appreciate the opportunity to appear before this subcommittee. It is always a privilege and an honor to represent the people of the Virgin Islands.

Today I want to speak to you as one legislator to another. I realize the very difficult task you have ahead of you in considering this legislation and in coming up with what will be best for the country as a whole, for the Caribbean countries, and for the territories as well. I feel sure that you, too, must be able to empathize with my situation in the Virgin Islands and with my responsibilities to the Virgin Islands people.

Some of my colleagues and I have worked diligently over the past ten months to assure the Virgin Islands a voice in the formulation of the Caribbean Basin initiative and to assure that the Virgin Islands be treated fairly under the initiative's policies. We have coordinated our efforts as much as possible with both Virgin Islands delegate Ron de Lugo and Governor Juan Luis. Our efforts have focused particularly on economic development for self-reliance in the belief that—all things being equal—the Virgin Islands can develop a much-needed diversity in its economic base.

During our first trip to Washington last June to plead our cause with administration officials and with Members of Congress, we met with one of the distinguished members of this subcommittee, my fellow Democrat James R. Jones from Oklahoma. Congressman Jones was very supportive of our efforts at that time. I hope we can count on him and on all of you to amend the administration's proposals adequately to create a truly favorable climate with the Caribbean Basin initiative so that the Virgin Islands will serve as a focal point for Caribbean commerce. In this way, the Virgin Islands can become a shining example of what free enterprise and free trade can mean to other Caribbean nations.

Self-reliance for the Virgin Islands within the greater social, economic, and political framework of the United States is a very attainable goal!

Virgin Islanders are loyal Americans. We have proved our loyalty continually during our 65-year relationship with the United States which began in 1917 when President Wilson purchased our islands from Denmark. Our men volunteered to fight in World War II even though they were not required to fight. Virgin Islanders have always held loyalty to be an honorable and admirable trait. We should not be hurt because we are loyal! We should be helped because the Caribbean is in turmoil, and we are a strategic and symbolic United States presence. We already represent the United States and the promise of America and democracy to many, many West Indians and West Indian countries. Our population includes citizens from nearly every island who have come to the Virgin Islands for a chance in life. That is why a healthy Virgin Islands is vital to the Caribbean and to the implementation and success of any Caribbean Basin initiative in which the United States plays a major role. That is why we must not be hurt by the administration's Caribbean Basin legislation. In fact, even the status quo is not going to be enough to maintain the Virgin Islands image in the Caribbean as one of solid and dramatic economic growth, creating opportunities for peoples from all over the Caribbean Basin. We must gain from such an initiative. We must be allowed—in fact we should be encouraged—to develop self-reliance and to reduce our present economic dependence on the United States. We are all aware of the regularity with which the Virgin Islands comes to Washington hat-in-hand for give-aways from the current administration and the Congress. We believe, however, that the heart and soul of the Reagan Administration's policies as well as of this distinguished subcommittee is to promote self-reliance in the interest of good fiscal management and economical development. More self-reliance is what the Virgin Islands wants and needs. However, we will need special assistance for this to develop in a positive manner which will reflect well upon the United States. Within the context of the CBI, however, we will need more favorable treatment than the beneficiary countries in order to succeed in the Caribbean and to continue to grow in stature as a symbol of what the United States and free trade among countries can do in the unified Caribbean. The bill before you will have the affect of taking away our competitive edge. This makes the Virgin Islands more likely to become too dependent upon the largess of the United States.

The current bill establishing the Caribbean Basin Economic Recovery Act would spell disaster for our economy if passed in its present form. It would shake the economic foundations of our community and create economic instability in a United States possession. This instability could lead eventually to social and political unrest. It could also shake the faith that Virgin Islanders have in America and the American system.

As it stands, the CBI is supposed to include trade, aid, and investment to create a unified Carribean under the banner of free trade. However, the thrust is all toward foreign countries. The investment benefits being extended to the other Caribbean counties are undercutting our heretofore privileged position in having the ability to lure investment. Trade is being set up, under this bill, to favor the other Caribbean countries because when the Virgin Islands is only being kept on a par with tax and free trade benefits to beneficiary countries, the Virgin Islands is, in fact, below par in its ability to compete in the Caribbean market place. As you will see, we have a number of major problems with this legislation as it is presently conceived.

Section 102, subsection (d) proposes to amend headnote 3(a) by adding the following paragraph: "(iv) subject to the provisions in section 103 of the Caribbean Basin economic recovery act, articles which are imported from insular possessions of the United States shall receive duty treatment no less favorable than the treatment afforded such articles when they are imported from a beneficiary country under such act." This may seem, on the surface, to benefit us, but it does not! Because the beneficiary countries all have cheap labor, lack of Federal regulations, and just as pleasant an environment to live in as we do, the major problem with this provision is that being on par with these beneficiary countries will make it impossible for us to compete favorably. When the other Caribbean countries with whom we will be in competition all have these advantages over us, then "no less favorable" treatment is not adequate.

Another problem we face with this bill deals with section 103, eligible articles. In order for imports to be eligible for duty free treatment, they must be imported directly from a beneficiary country into the customs territory of the United States. Also the sum of the cost or value of the materials produced in a beneficiary country or two or more beneficiary countries plus the direct cost of processing operations performed in such beneficiary countries is not less than twenty-five percent of the appraised value of the imported item. We have no raw materials to add as part of the 25 percent Caribbean value added being proposed. Further, we have no ability to compete for labor intensive processing, because the other islands have a much cheaper labor pool to use.

The "snap back" provision—Subsection (d)(2) does not hold any real protection for the Virgin Islands, though we are considered domestic for the purposes of this subsection which does allow for the Virgin Islands to be eligible for import relief if there is serious injury to a domestic industry substantially caused by imports of articles receiving duty-free treatment under this title. The problem with this provision is simple. Except for watches and rum we might have no serious injury possible in the sense of this subsection. The serious injury will come to the Virgin Islands in a different form—that of not being able to establish industries at all. The "snapback" provision does not allow for that, therefore it is not going to provide adequate protection for the Virgin Islands in the areas in need of protection.

Section 104, measures for Puerto Rico and U.S. insular possessions, provides for an additional liter of duty-free liquor to be imported by each person exiting the Virgin Islands. This token gesture, will not even begin to make up for the damage otherwise being done to us by this measure. Also, the provision to protect the rum industry states only that "the President shall consider compensatory measure and . . . may withdraw the duty free treatment on rum provided by this title." The key words are "may withdraw." Without the protection being automatic, there is too much discretion given to the President to make the provision good protection for us.

Further, there are things which have been promised to us but are not included in this section or in this bill. For example, in the "Caribbean Basin Policy Fact Sheet" it says that "Puerto Rico and the U.S. Virgin Islands will play a major role in technical assistance, private sector development, and transportation within the Caribbean region. As a part of the Caribbean Basin initiative, the administration will seek congressional authoritzation for the following measures to foster the development of Puerto Rico and the Virgin Islands.

For the Virgin Islands, funding for an eastern Caribbean center for educational, cultural, technical, and scientific interchange at the college of the Virgin Islands.

Use of Puerto Rico and Virgin Islands facilities, personnel, and firms in technical assistance programs and development projects.

Expansion of airports in the Virgin Islands and other measures to encourage the development of Puerto Rico and the Virgin islands as a transportation hub for the Caribbean region.

None of these provisions actually appear anywhere in this bill.

Section 201 emergency economic assistance excludes the Virgin Islands entirely. According to the"fact sheet", last July when Secretary of State Alexander Haig and U.S. Special Trade Representative William Brock III met in Nassau with the foreign ministers of Canada, Mexico, and Venezuela, they agreed to sponsor a multilateral action program for the region within which each country would develop its own program. Venezuela and Mexico are making contributions to the Caribbean Basin, particularly through their joint oil facility. Canada recently announced increases in aid. The Columbians and others are also interested in expanding their efforts. The Caribbean Basin initiative is the basis for the U.S. program. But we get none of your emergency economic assistance though we need it as badly as anyone else. We will get neither oil nor foreign assistance from these other countries. Yet the Caribbean countries around us will get both oil and foreign assistance as well as economic assistance from the U.S. and other benefits through this legislation which puts them on a more favorable basis than the Virgin Islands.

Investment tax credit and accelerated cost recovery are nothing new for the Virgin Islands. Under our mirror theory tax system which reflects the same rules and regulations as the Federal system, we already have them. All this section does is further erode our advantages over other Caribbean countries, giving us nearly nothing in return.

Oil refining. Tourism. Rum. These are the foundations of the Virgin Islands economy.

First, Hess Oil Virgin Islands Corporation is the major industrial contributor to the Virgin Islands treasury. Hess recently filed its corporate income taxes for 1981. The corporation shows substantial losses and will carry them forward, so we cannot predict with any accuracy what revenues, if any, we can expect from Hess in the near future. Given the worldwide oil clut which now exists and the fact that Hess Oil Virgin Islands Corporation has substantial losses, the government of the Virgin Islands faces the distinct possibility of not receiving corporate income taxes from its biggest taxpayer for the predictable future.

Second, with regard to tourism, the beneficiary countries all have the same Sun, sand, and sea, and tourism in the Virgin Islands is experiencing a down-turn, even with vigorous promotion. To some extent this is probably due to the recessionary trends in the states which accounts for the lion's share of our tourist trade. This is beyond our control; but another area which is hurting tourism is our decreasing competitiveness as a shopping port for tourists. The tourism reputation of St. Thomas and the Virgin Islands generally has always been that of a "Free Port" with bargains and prices better than other places. The price advantages were due primarily to the fact that tariffs on a large variety of items were considerably lower in the Virgin Islands than they were in the United States. Over the past twenty years, tariffs on many of these items to the United States have either been eliminated or have been reduced very substantially. Thus, the competitive advantage enjoyed by the Virgin Islands has been lost, and on a number of items, such as electronics and camera equipment, merchants in the islands are no longer able to compete with prices available in the United States or in surrounding competitive markets.

Rum is one of our oldest and most reliable industries. Its importance is also critical to our economy. The industry provides approximately 80 jobs for our people. That's a lot of jobs for a territory of only 95,000 people according to the last official census. As the Governor stated earlier, the excise tax which is returned to us each year on rum imported into the United States amounts to $37.1 million or 15 percent of the Virgin Islands budget. That money is earned through our own local rum production.

Frankly we are concerned about receiving the excise taxes on rum produced by other countries as is proposed by the legislation before this subcommittee. That is proposed by the legislation before this subcommittee. That is revenue which we did not earn! It is, in essence, another hand-out, and will only foster dependnecy. Ten years from now another David Stockman may come along and ask why we receive excise taxes on other countries' rum. He may want to cut out that kind of rebate to the Virgin Islands when he finds out that the Virgin Islands has no claim on that money. I think, gentlemen, that all of the safeguards and guarantees will be of no avail if there is no growth potential for the rum industry in the Virgin Islands or if the wisdom of a future administration or Congress dictates that the Virgin Islands should no longer receive the rebate on foreign rum excise taxes which the Virgin Islands did not earn!

We do have a right to the excise taxes we get on rum which we produce in the Virgin Islands. However, it seems to me that the proper approach would be to exempt rum from the free trade area completely! That's the only way to safeguard and guarantee our rum industry's potential for growth. Short of total exemption, at least set the policy in such a manner as to foster growth in the industry, not stagnation and possible loss of the industry. A meaningful quota system might be an answer to gradual industry adjustment for the Virgin Islands. For example, rum might remain exempt from the free trade area for the first five years. Then, a gradually increasing system of quotas on duty free foreign run imports could be instituted. This would give the Virgin Islands the opportunity to make the adjustments necessary for a time when rum from other Caribbean countries may become more competitive. However, that time will not be coming tomorrow or next year! That would be too fast! We are, after all, a truly developing country just as surely as these other Caribbean countries are. We are further along, but still in great need of the basic supports and advantages our relationship with the United States has always afforded. Even the smallest of our industries is critical because of our microeconomy. This kind of approach would also protect our rum industry completely for a period of years before the free trade quotas on foreign rums would go into affect. Tha way we continue to earn our excise taxes at the same basic level for a long enough time for us to prepare for the possibility of losing some of those taxes because of a drop in sales.

There are possible solutions as well to other problems we have with the Caribbean Economic Recovery Act. After all, American policies were instrumental in developing our economy especially the tourist shopping market. Together we must seek ways of making the Virgin Islands once again competitive in the Caribbean market. Some of this can be done, and is being explored, locally. Here, you can help by supporting such congressional efforts as H.R. 5113 which would reduce to 10 percent from 30 percent the tax rate on dividends, interest, and other passive income flowing from the Virgin Islands to the United States and which would remove foreign tax credit restrictions as they relate to this tax. H.R. 5113 was introduced by Delegate de Lugo.

You can give us some assistance in another area by amending the CBI legislation to include the Virgin Island in the American Customs territory for purposes of receiving duty-free imports from the Caribbean Islands to trans-ship to the States through the utilization of the new container port in St. Croix. The Virgins Islands could truly be a center for import/export and trans-shipment trade between the Caribbean and the United States as well as other parts of the world. Howerver, in order to achieve this we must have these kinds of concessions.

Section 103, eligible articles, can be amended to require that Caribbean goods pass through the Virgin Islands as a part of the value added formula. For example, if goods are shipped directly from a beneficiary country to the customs territory of the United States, then the goods would be, say, 75 percent duty free. If the same goods came through the Virgin Islands, the goods would gain the additional 25 percent duty exemption so that the goods enter the United States 100 percent duty free. Just take a moment to consider the many spin-off businesses, the vast potential for commerce which this idea would provided for a U.S. territory.

The "snap back" provision must reflect our lack of natural resources and our needs before it can do us any good. It must somehow safeguard industrial development in the Virgin Islands as an entity, not just individual industries which are in trouble because of the basin initiative. There is no protection for businesses not locating in the Virgin Islands because of benefits to beneficiary countries. The "snap back" concept must broadened to include an injured state or territory.

According to the administration, the overall objective of the Caribbean basin initiative is to expand the productive sector to enable nations to increase their resource base, provide employment, and move toward economic self-sufficiency. Yet we notice, with some chagrin, that the Virgin Islands is excluded from the $350 million appropriation for emergency economic assistance. Well, that's okay with us as long as we get some compensatory program to do for us at least what is being done for the non-U.S. areas: and there is another way of funding low interest development loans and capital improvements and for rebuilding infra-structure with earned dollars, not give-aways. The source of funds is gasoline excise taxes on a product produced in the Virgin Islands. That is money we've earned!

And we desperately need such additional sources of revenue in order to adjust and move our economy in a self-sufficient and postive growth-oriented direction.

The small business administration, economic development administration, and the farmers home administration are being cut back to such an extent that there is little funding available for infra-structure improvement. Such improvement is needed desperately if we are ever going to get industry to establish in the Virgin Islands. Ports, water and power, and more specialized and sophisticated systems of accounting are needed: Yet we are unable to get assistance from sources outside of the United State's Federal programs. Also, companies and industries wishing to invest in the Virgin Islands are unable to obtain low-interest loans from the world bank, Inter-American development bank, international monetary fund, international bank for reconstruction and development, and other international financial institution.

With regard to tax considerations such as the investment tax credit and accelerated cost recovery, if concessions such as these are given to other Caribbean countries, then the Virgin Island must be given additional benefits over and above the tax benefits which we already enjoy.

That is the kind of edge we must maintain over the Caribbean competition we face with the passage and implementation of any type of Caribbean Basin free trade or open trade concept. Congress must remember that the Virgin Islands will not survive as a stable political entity and territory of the United States of America if you do not assist us in every way possible to keep our competitive edge. Our success can only serve to enhance the credit of the United States of America.

Distinguished members of this subcommittee. Mr. Chairman. My remarks are in the spirit of cooperation. They are meant to be informative in nature, so that you may have the direct input of Virgin Islanders as you consider the Reagan administration's Caribbean Basin Economic Recovery Act. I have been and will continue to be, at your service in any manner I can. I am willing to discuss these various items I have mentioned and any other provisions of the legislation in detail with any of you at any time. The urgency of the situation in the Caribbean demands action. The right action must be an action or series of actions and policies which lead to helping all of us in the Caribbean and which provide a continuing special assistance component for the Virgin Islands in order that we may grow and develop into the zenith of free enterprise, free trade, and democracy in the Caribbean. What better result could come from a Caribbean Basin initiative than to have such a bastion, such an outpost, of free enterprise and democracy as the leader of the economically unified West Indies. The Virgin Islands is the natural for this role. Your investment in us is already substantial. In order that it pay off big dividends, I strongly recommend that you scrutinize this legislation very carefully for vague language and loopholes for the other Caribbean countries before you act. You are the last hope. The economic well-being of the Virgin Islands is in your hands. The fate of the Caribbean is in your hands. It is a grave and burdensome responsibility. We are willing to do whatever we can to shoulder some of that burden with you, but we must be in shape to do so. We must become self-sustaining economically. The potential for that growth also rests in your hands.

Thank you.

Chairman **Gibbons**. Senator Williams, you have a very fine and a very forceful statement.

Senator **Williams**. Thank you.

Chairman **Gibbons**. Next is the chairman of the Committee on Agriculture.

STATEMENT OF HON. BENT LAWAETZ, VICE CHAIRMAN, COMMITTEE ON COMMERCE, LEGISLATURE OF THE VIRGIN ISLANDS

Senator **Lawaetz**. Thank you, Mr. Chairman.

I thank you for this opportunity to testify on the proposed Caribbean Basin Recovery Act.

My name is Bent Lawaetz. I am a member of the Virgin Islands Legislature, where I am vice chairman of its committee on commerce. I am also a member of the Governor's task force on the Caribbean Basin Initiative, and I have participated in negotiations on the Caribbean Basin Initiative from the very beginning.

The Virgin Islands would be a major beneficiary of the Caribbean Initiative to the extent that the program might bring increased economic and political stability to the region. For that reason, I would very much like to support the initiative, but as an elected representative of the people of the Virgin Islands, I cannot support legislation which so clearly would harm the people I represent.

Many of the sections in the proposed legislation which are harmful to the Virgin Islands could have been made acceptable had adequate compensatory measures been included in the proposed legislation, but those compensatory measures which had been requested are sadly missing from the proposal. We have been told that most of those issues will be dealt with outside the CBI, but I cannot support the CBI on the hope that those other measures will be dealt with favorably after the CBI is in place.

Those other measures needed for the welfare of the Virgin Islands would either have to be locked into the CBI or passed concurrently in order for me to support the proposed Caribbean Basin Initiative legislation.

The main protection measures I am seeking for the Virgin Islands are: One, more protection for the rum industry by (a) waivering the EPA requirement to build a $5 million treatment plant for the effluent from the distillery, (b) installing a quota system to preclude major disruptions in the market, (c) including Virgin Island rum in Protocol No. 7 of the Lome Convention of 1975 in order to make our rum industry competitive in the European market; second, passage of H.R. 5758, a bill to amend the tariff schedules of the United States with respect to the dutiable status of watches and watch movements from insular possessions of the United States. Between 600 and 800 jobs in the Virgin Islands depends upon the passage of that bill.

At this point, Mr. Chairman, I would like to divert a moment from my written testimony to address a concern raised this morning regarding having the watch industry develop into a passthrough operation in the Virgin Islands. According to the proposed bill, the watch industry in the Virgin Islands would be subject to labor input requirements as set out by regulations promulgated by the Department of Commerce and that would preclude it from becoming a passthrough operation.

The third item we have sought is passage of H.R. 2232, a bill to revise the headnote 3(a) program. Even without passage of the CBI legislation, we are not able to attract investments in the Virgin Islands because of the existence of this 30-percent withholding tax. It is essential that both sections of this bill be passed.

Fourth, it is essential that headnote 3(a) of the tariff schedules of the United States be amended to change existing foreign component limitation of 50 percent to 70 percent. Without this change, we would not become competitive with our neighboring islands because of the liberal trade policies being extended to them.

Fifth, the excise taxes collected on gasoline should be returned to us, just as the excise tax collected on rum is presently returned to us. We urgently need this source of funding to develop our airports, harbors, water and power production and distribution systems and other aspects of our infrastructure.

This source of funding would also be used to fund a development bank which would enable us to offer the types of financial services presently available to the neighboring islands and countries through the World Bank and other international financial institutions.

Although we appreciate very much the grants which the U.S. Government has given us for some of the above items, the funding procedure leaves us in the position of having to beg for everything we get. Gentlemen, it is no fun to be a beggar. It leads inevitably to feelings of bitterness and resentment.

The taxes which I am referring to are taxes on products which we produce and which I believe the Congress intended to be returned to us when they passed the Revised Organic Act of 1954.

Six, the Virgin Islands are generally excluded from tax treaties negotiated between the United States and foreign countries. This makes it almost impossible for us to attract foreign investments which would help to strengthen and diversify our economy.

These are just some of the major issues that we have negotiated for unsuccessfully.

At this time I would ask to have included in the record the editorial of Monday, March 22, 1982 of one of our local newspapers, the St. Croix Avis, which is attached to my testimony.

Chairman GIBBONS. Yes, sir, we will include it.

[The editorial referred to follows:]

The St. Croix Avis
Serving The Virgin Islands Since 1844

Fred Clarke — Publisher & Editor
Monique Clendinen — Managing Editor
Lydia A. Smith — Business Manager

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May 26, 1917 under the Act of March 3, 1879

MONDAY, MARCH 22, 1982 No. 67

EDITORIAL:

WAR AND PEACE

WE MUST BE doing something wrong. Possibly, we are doing some thing right instead of doing something wrong. And that could be the reason the U.S. Virgin Islands is being, more or less, overlooked in the President's Caribbean Basin Initiative program.

WE ARE NOT at war and the only time, since the Virgin Islands became part of the United States of America that the men and women of the Virgin Islands engaged in any wars, was to help the United States. And that help was given, willingly and for the most part, voluntarily, during every conflict the United States has been engaged since World War I.

YET, MAYBE THAT is what we're doing wrong. We are not at war with our neighbors or within our own boundaries. It seems the bulk of the billions of dollars to be expended under the Caribbean Basin Initiative will be poured into those nations or countries involved in bloody wars, international or insular communistic or civil.

MILLIONS AND MILLIONS of dollars to arm and aid the troops in El Salvador to battle Salvadorean rebels. And millions more will go to Nicaragua which reportedly is pouring arms and aid to support those same rebels.

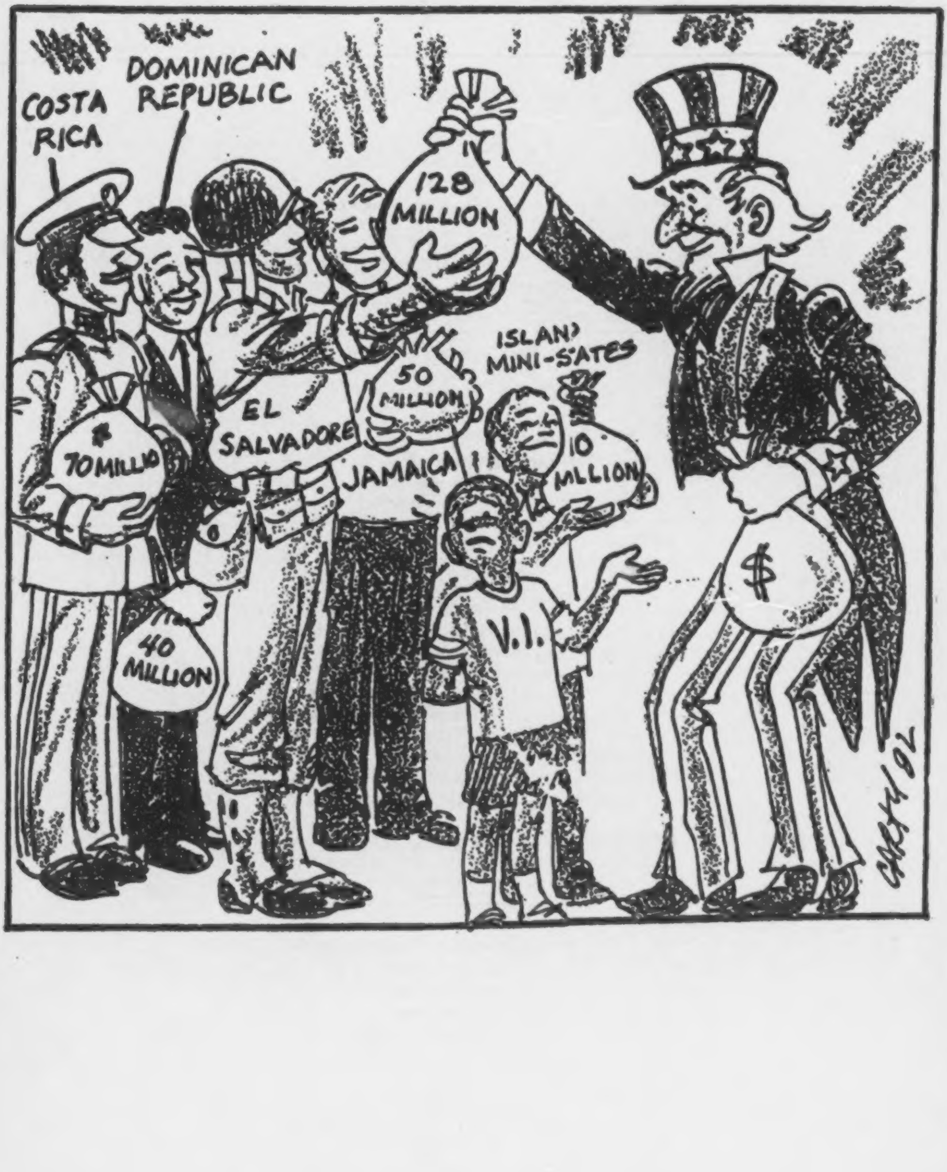
WE HAVE OUR difficulties between islands. We battle on the floor of the Legislature, and we toss complaints and challenges back and forth across the 40 miles of water separating us. But, each day, we take pride in the fact that we are all Virgin Islanders and in the belief we can settle our problems without guns, tanks, riots and revolution.

YET, WE ALSO need help. We are small, we are dependent upon assistance from the United States not to exult but to exist. We ask for help and many times our leaders and representatives have to beg for aid. Not arms.

SO, WE MUST be doing something wrong. Under the Caribbean Basin Initiative, our students will have to forego school lunches so the Salvadoreans can better feed their troops. Our needy will go hungry so Nicaragua can better spread its hatred. Our pledge of allegiance is forgotten while Washington hears promises of forced friendship.

OH, YES. WE must be doing something wrong. Or, again, maybe it's because we're doing something right that we are being placed in the wrong light. Apparently, the brightest light, the most attention, shines on War. Peace is pushed off stage.

IT MAKES YOU FEEL LIKE AN ORPHAN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Senator **Lawaetz**. I was born in the Virgin Islands. I have lived there most of my life. Now for the first time in my life I am hearing Virgin Islanders question the wisdom of being a U.S. territory. Historically we have been a stabilizing influence in the Caribbean, a shining light of democracy and Americanism. I appeal to you, do not extinguish our light.

Thank you, Mr. Chairman.

Chairman **Gibbons**. Thank you, sir, for your very fine statement, and I have some questions I need to ask you about line 2, page 3, paragraph 5. As soon as we hear the other witnesses, we will come back to that.

Mr. Southerland.

STATEMENT OF JAMES SOUTHERLAND, PRESIDENT, ST. CROIX CHAMBER OF COMMERCE, U.S. VIRGIN ISLANDS

Mr. **Southerland**. Mr. Chairman, my name is Jim Southerland. I am president of the St. Croix Chamber of Commerce, and I, too, am a member of the Governor's Task Force on the Caribbean Basin Initiative.

As a representative of the private sector of the U.S. Virgin Islands, I want you to know that the business community is grateful for this opportunity to present its views on President Reagan's Caribbean Basin Initiative, and to also assure you of our concurrence with the earlier testimony by our Governor, our Delegate, and these two distinguished Senators.

I have read and reread the President's speech to the Organization of American States, and the more I study it, the more I am impressed with the wisdom and eloquence in the message he delivered. I am especially encouraged by the words near the end where he said, "The Western Hemisphere does not belong to anyone of us; we belong to the Western Hemisphere. We are brothers historically as well as geographically."

I believe that my country is now ready to go beyond being a good neighbor to being a true friend and brother in a community that belongs as much to others as to us. That, not guns, is the ultimate key to peace and security for us all.

Despite these words indicating an understanding of the Caribbean Basin, I must tell you the private sector of the U.S. Virgin Islands is nervous about the way these words will be translated into deeds. In the past we have felt that Washington often overlooked this region and its vital strategic and potential commercial contributions.

Perhaps the oversight was the result of its close proximity to the shores of the U.S. mainland. We are pleased that our country is taking an active interest in this area of the Western Hemisphere. As the CBI is implemented by this and other legislation, we the people of the U.S. Virgin Islands must be provided the opportunity to develop and expand our economy.

As I am sure you are aware, our Caribbean neighbors' perception of the United States is formed as much from what they see taking place in the U.S. Virgin Islands as it is from what they observe on the more distant mainland. We the U.S. Virgin Islands are the United States to our Caribbean Basin neighbors.

On the Island of St. Croix, the business community is comprised mostly of small businesses. Eighty percent employ 15 or fewer persons. But we have the start of a vital industrial base that contributes greatly to our economy and stability. As you have been told, the largest industries are Hess Oil Virgin Islands Corp., Martin-Marietta Alumina, Virgin Islands Rum Industries, Ltd., and several watch assembly plants. These provide many jobs and contribute millions to our economy.

The principal ingredients needed to diversify and encourage growth in our private sector economy are simple. We have three basic needs. Our first requirement is for capital. Being a part of the United States and at the same time competing with the other basin countries and islands, we are at a disadvantage in obtaining capital. Our only source of startup or expansion capital is high interest money from commercial banks when and if it is available.

Other countries and islands, except, of course, Puerto Rico, in the basin and whose economy is to be aided by this legislation have access to low interest funds from several sources, such as the Export-Import Bank, the Inter-American Development Bank, the Caribbean Development Bank, et cetera. We in the U.S. Virgin Islands are barred from participating in these sources of funding.

If we the U.S. Virgin Islands are to assure the leadership role necessary for the CBI to be a success, we must have low interest capital development funds available, and we strongly suggest that a territories development bank is a solution.

The second basic need of the private sector is in the area of the island's infrastructure. We have a sporadic, unreliable water and power system, and we need to upgrade our crime fighting ability. While making funds available to others within the basin, the Congress and administration must insure that the U.S. Virgin Islands have funds to improve these areas.

The importance of these two ingredients by business was emphasized just a few weeks ago when two experts, David Burch, director of the Massachusetts Institute of Technology's program on neighborhood and regional change, and Stewart Butler of the National Center for Neighborhood Enterprises, testified on why businesses invest in an area.

They told the Senate Small Business Committee the two most important items are startup capital availability and a crime-free environment.

Our third need is exemption from certain regulations, especially those of the Environmental Protection Agency, that serves only as a costly nuisance, as in the case of the Virgin Islands rum industry being required to install a treatment facility for their discharge, which biologists have testified does not harm the environment but does feed the fish in the sea.

In short, as investment incentives are granted to Caribbean countries, we must have low interest capital available, financial help to insure a sound and reliable infrastructure, and exemptions from some unneeded regulations which do not exist in the other islands.

Further, we believe the U.S. Virgin Islands must be permitted to participate in all of the CBI bilateral investment treaties which may be initiated. What the President called the centerpiece of the

CBI legislation, free trade for Caribbean Basin products, contains no provisions for the U.S. Virgin Islands to export its products, now or in the future, to its neighboring countries under the same tariff conditions their exports are received. This should be corrected.

Rum is a traditional product of the Virgin Islands, and it is an emotional issue as much as an economic one. As you have been told, it is a large contributor to our government. We believe that some accommodation must be made in this area of the legislation. Importation of duty-free rum from all the basin is a very real threat to the U.S. Virgin Islands rum industry because of the competitiveness of this Caribbean product and the unique marketing of our rum, as you now are aware.

Our belief is that rum should be exempt from this legislation and accorded the same treatment as textiles. We believe a quota system would benefit all the Caribbean Basin. In his message, President Reagan said, "We will propose special measures to insure that they—that is, Puerto Rico and the U.S. Virgin Islands—also will benefit and prosper from this program."

In order to fulfill this commitment, a method of meeting and accommodating the needs of the private sector of the U.S. Virgin Islands must be reached with this and other legislation.

Just over 20 years ago, President Kennedy made a speech similar to President Reagan's OAS speech in which he said that if the United States could not inspire peaceful revolution in Latin America, it would surely have to deal with a violent revolution. I do not believe that our area, the eastern Caribbean, has the same explosiveness as is now taking place in the western area, but I do believe this entire region must have the opportunity to grow and prosper so that social and economic conditions do not produce the same violent actions.

Finally, if the United States is serious about continuing its leadership role in the Caribbean Basin, we the U.S. Virgin Islands must continue to be a leader among our neighbors. If we are not permitted to fulfill this role, the entire Caribbean Basin Initiative will be a mockery. We are the United States in the Caribbean.

I thank you, Mr. Chairman.

Mr. **Gibbons**. Thank you, Mr. Southerland, for a very fine statement. As I said before, I have visited that area, but a visitor doesn't learn nearly as much as he learns by listening to you.

Mr. **Southerland**. Thank you.

Mr. **Gibbons**. Ms. Creque?

STATEMENT OF MARGARET L. CREQUE, FIRST VICE PRESIDENT AND PRESIDENT-ELECT, ST. THOMAS-ST. JOHN CHAMBER OF COMMERCE

Ms. **Creque**. Thank you, Mr. Chairman.

I am Margaret Creque. I am the first vice president and president-elect of the St. Thomas-St. John Chamber of Commerce, and chairman of its Government affairs committee. I am also a member of Governor Juan Luis's tax force on CBI. I am an automobile dealer in Charlotte Amalie on the island of St. Thomas.

The St. Thomas-St. John Chamber of Commerce is truly honored to be given this opportunity to present its views on the Caribbean

Basin Economic Recovery Act and its impact on the territory of the U.S. Virgin Islands.

We applaud the President's policy of providing assistance to the Caribbean countries, but we urge great caution that the U.S. Virgin Islands as "the U.S. showcase of democracy" in the Caribbean not be sacrificed in the process. As we listened to the President's remarks to the Organization of American States on February 24, 1982, we were pleased to hear him say that special measures would be taken to insure that the U.S. Virgin Islands benefit and prosper from his program of free trade for the Caribbean Basin products exported to the United States. We were further gratified by the statement that Puerto Rico and the U.S. Virgin Islands economic development will be "enhanced" by the U.S. policy toward the Caribbean region.

However, as we now see how this enhancement is to be accomplished, it is evident to us that greater consideration has to be given to the U.S. possessions in the Caribbean than is envisioned in the proposed plan.

Economic diversification has always been one of the objectives of the territory. The fragility of the tourism industry dictates that the economic base be broadened through futher investments in the territory. However, opening of free trade between other Caribbean countries and the United States means increased U.S. investments in those countries. Investments in those countries will become far more attractive to American businessmen because they do not have to be concerned with U.S. minimum wages, with OSHA, with the Clean Air Act, Environmental Impact Studies, and Coastal Zone management requirements. The U.S. Virgin Islands have to adhere to all of the applicable U.S. laws.

An additional deterrent to investment in the U.S. Virgin Islands not encountered in the rest of the Caribbean is the provision of the 30 percent withholding tax on passive income earned in the U.S. Virgin Islands. Passive income in many Caribbean islands is subject to only 5 percent to 15 percent withholding tax, based on tax treaties with the U.S. Government. Therefore, we urge that H.R. 5113 introduced by Delegate de Lugo be made a part of the CBI Act if not passed beforehand, so that the U.S. Virgin Islands will be competitive in attracting and retaining investment for economic diversification in our islands.

These conditions indicate to us that the very economic survival of the U.S. Virgin Islands is threatened by the Caribbean Basin Initiative program. We see nothing in the proposed legislation before the Congress that addresses this very serious problem.

Mr. Chairman, I would like to add that I spoke to the Virgin Islands Department of Commerce yesterday morning before I left St. Thomas, and in particular questioned the Industrial Development Commission as to the status of new investment and industry they have brought to the Virgin Islands. I was told that we simply are not attracting new industry, especially labor-intensive industry, inasmuch as we already are not competitive with other Caribbean islands.

This problem is due greatly in part to the 30-percent withholding tax, Federal regulatory measures, and Federal minimum wages. In fact, there has been a 5.2-percent decline in employment during the year of 1981 in the manufacturing sector. It is most apparent to us that the measures contained in the Caribbean Basin Economic Recovery Act will further seriously erode our ability to attract investment and diversify our economy, unless the safeguards proposed by Delegate de Lugo and Governor Juan Luis are incorporated into this act.

The removal of U.S. tariff barriers on rum imported from beneficiary countries presents another very serious problem to the economic survival as a territory. Currently, the rum industry in the U.S. Virgin Islands is the largest single source of revenue. It generates close to $40 million in revenues to the government and provides over 100 jobs. In a small territory as the Virgin Islands, $40 million and 100 jobs are of great significance.

Again, the proposed Caribbean Basin Economic Recovery Act now before the Congress does not in our estimation adequately address our rum situation. The act proposes to compensate the U.S. Virgin Islands for any loss in revenues that may, and I underline the word "may," result from a reduction in Virgin Island rum sales by rebating additional excise taxes collected on foreign rum imported into the United States, and that if such taxes are not rebated, the tariffs would "snap back" to their original levels.

This posture clearly leaves the U.S. Virgin Islands at the mercy of the behavior of the other Caribbean countries. section 104(b) of the act does not provide any real tradeoff for the Virgin Islands or Puerto Rico. Words such as "shall consider" or "may withdraw" mean nothing in the context.

It seems to us the damage would be so catastrophic if such rebates were not made that post facto remedies will be too late to salvage our economy. We simply cannot afford to take this risk. We believe that consideration should be given to a quota system that would allow for the phasing in of duty-free provisions of foreign rum exported to the United States by beneficiary countries other than the U.S. Virgin Islands.

We are also concerned that the amendment to the general headnote 3(a) to the tariff schedules of the United States does not do very much for the U.S. Virgin Islands. The inclusion of beneficiary countries into the provisions of headnote 3(a) in section 103(a)(1) of the act will effectively remove any headnote 3(a) business from the U.S. Virgin Islands.

Our legal relationship with the Federal Government as a territory of the United States dictates a great deal of dependence upon foreign assistance. The President advocates a lessening of such dependence by the State and territories. This simply means that we are going to have to do more about our economic development. To do so, however, will require immediate Federal assistance enabling us to strengthen our infrastructure. Airports, shipping ports, highways, electrical power and water production facilities all have to be improved in order to provide the basic necessities to attract potential investors to our shores.

In this regard, we applaud the administration's support for continued funding of the airport expansion project.

The U.S. Virgin Islands are not eligible for loans from the World Bank, Eximbank, and other international financial institutions. Therefore, we believe that the creation of the U.S. Virgin Islands

Economic Development Bank, funded by the return of gasoline excise taxes, will assist in enabling us to be less dependent upon the Federal Government. It will be able to provide financing for both infrastructure as well as investment.

The St. Thomas-St. John Chamber of Commerce recognizes the fact that any action that will give equal treatment to our Caribbean competitors will create an unequal condition and loss of competitive edge for the U.S. Virgin Islands. We urge that this subcommittee consider what will happen to the U.S.'s showcase of democracy in the Caribbean if they are not given special consideration in the Caribbean Basin Economic Recovery Act.

Thank you, Mr. Chairman.

[The prepared statement follows:]

STATEMENT OF MARGARET L. CREQUE, FIRST VICE PRESIDENT, ST. THOMAS-ST. JOHN CHAMBER OF COMMERCE, INC.

Mr. Chairman, and honorable members of this subcommittee. I am Margaret L. Creque, First Vice President of the St. Thomas-St. John Chamber of Commerce and Chairman of its Government Affairs Committee. I am an automobile dealer in Charlotte Amalie on St. Thomas. The St. Thomas-St. John Chamber of Commerce is truly honored to be given this opportunity to present its views on the Caribbean Basin Initiative's impact on the Territory of the U.S. Virgin Islands.

We applaude the President's policy of providing assistance to the Caribbean countries, but we urge great caution that the U.S. Virgin Islands as, "the United States showcase of democracy" in the Caribbean not be sacrificed in the process.

As we listened to the President's remarks to the Organization of American States on February 24, 1982, we were pleased to hear him say that special measures would be taken to ensure that the U.S. Virgin Islands benefit and prosper from his program of free trade for Caribbean Basin products exported to the United States. We were further gratified by the statements that Puerto Rico and the U.S. Virgina Islands economic development will be enhanced by the U.S. policy toward the Caribbean region.

However, as we now see how this enhancement is to be accomplished, it is evident to us that greater consideration has to be given to the U.S. possessions in the Caribbean than is envisioned in the proposed plan.

Economic diversification has always been one of the objectives of the Territory. The fragility of the tourism industry dictates that the economic base be broadened through further investments in the Territory. However, opening of free trade between other Caribbean countries and the United States means increased U.S. investments in those countries. Investments in those countries will become far more attractive to American businessmen because they do not have to be concerned with U.S. minimum wages, OSHA, the Clean Air Act, Environmental Impact Studies, and Coastal Zone Management Requirements, (to name a few). The U.S. Virgin Islands have to adhere to all the applicable U.S. laws.

An additional deterrent to investment in the U.S. Virgin Islands not encountered in the rest of the Caribbean is the provision of the 30 percent withholding of passive income earned in the U.S. Virgin Islands.

These conditions indicate to us that the very economic survival of the U.S. Virgin Islands is threatened by the Caribbean Basin Initiative program. We see nothing in the proposed legislation before the Congress that addresses this very serious problem.

The removal of U.S. tariff barriers on rum imported from beneficiary countries presents another very serious problem to the economic survival of the Territory. Currently the rum industry in the U.S. Virgin Islands is the largest single source of revenue. It generates close to $40 million in revenues to the Government and provides over 100 jobs. In a small territory as the U.S. Virgin Islands, $40 million and 100 jobs are of great significance.

The revenues are used to satisfy general obligations of the local government and account for approximately 20 percent of all revenues received by the Government.

Right now, the federal excise taxes collected on rum sold on the mainland by U.S. Virgin Islands manufacturers are rebated to the local treasury.

Again, the proposed Caribbean Basin Economic Recovery Act now before the Congress does not, in our estimation, adequately address our rum situation. The Act proposes to compensate the U.S. Virgin Islands Government for any loss in revenue that may result from a reduction in Virgin Islands rum sales by rebating additional excise taxes collected on foreign rum imported into the U.S.; and that if such taxes are not rebated the tariffs would "snap back" to their original levels. This posture clearly leaves the U.S. Virgin Islands at the mercy of the behavior of the other Caribbean Countries. The "safe guards" provided in the Act only go into effect after the fact. However, it seems to us that the damage would be so catastrophic if such rebates are not made that *post facto* remedies will be too late to salvage our economy. We simply cannot afford to take this risk.

There seems to be some thinking by the Administration that the rum industry in Puerto Rico and the U.S. Virgin Islands is the same. The fact, is most of the rum produced in the U.S. Virgin Islands is the less expensive unaged bulk rum sold primarily to rectifiers who age and bottle it and then apply their own brand labels.

Puerto Rico, on the other hand, produces and sells a finished product with its own label, as is in the case of Bacardi. The difference lies in the lack of exposure of Virgin Islands rum in the U.S. rum market. As a result, the rebate formular suggested would have a far greater adverse impact on the U.S. Virgin Islands than on Puerto Rico.

We are also concerned that the amendment to the General headnote 3(a) to the Tariff Schedules of the U.S. (19 U.S.C. 1202) does not do very much for the U.S. Virgin Islands. In providing equal treatment to the other members of the Caribbean Basin, the U.S. Virgin Islands is rendered less competitive. We believe that consideration should be given to a quota system that would allow for the phasing-in of duty-free provisions of foreign rum exported to the U.S. by beneficiary countries other than the U.S. Virgin Islands.

Our legal relationship with the Federal Government as a Territory of the United States dictates a great deal of dependency on Federal assistance. The President advocates a lessening of such dependency by the States and Territories. This simply means that we are going to have to do more about our own economic development. To do so, however, will require immediate federal assistance enabling us to strengthen our infra-structure. Airports, shipping ports, highways, electrical power and water production facilities, all have to be improved in order to provide the basic necessities to attract potential investors to our shores.

In this regard, we applaud the Administration's support for continued funding of the airport expansion project.

We also believe that the creation of an Economic Development Bank funded by the return of gasoline excise taxes will assist in enabling us to be less dependent on the Federal Government.

The St. Thomas-St. John Chamber of Commerce recognizes the fact that any action that will give equal treatment to our Caribbean competitors will create an unequal condition and lost of competitive edge for the U.S. Virgin Islands. We urge that this subcommittee consider what will happen to the U.S. showcase of democracy in the Caribbean if they are not given special consideration in the Caribbean Basin Economic Recovery Act.

Mr. GIBBONS. Thank you.

I want to thank each one of you for your very fine statements, and for the candor with which you state your problems, and the fairness with which you state your problems. I think they have been marked by a great deal of understanding of the overall problem, and yet a healthy statement of your own self-interest. We must consider that.

When we undertook the first consideration of this bill, a question that always hounded us was, what impact will all of this have upon Puerto Rico and the Virgin Islands? It is obvious to me that the concern of you from the Virgin Islands and some of the witnesses from Puerto Rico is, it will have a serious impact upon your ability to compete, and I hope that we can, as we work on this legislation, do something about that.

I realize you have a problem. We don't want to change your minimum wage laws. We don't want to change some parts of your OSHA laws or your environmental laws, because changes there might bring about more abuses than they would correct. I don't know what kind of effluent comes out of a rum plant, but I don't see where it would do too much harm to the acquatic environment around the plant. The plant has been there for some time, has it not?

Mr. **Lawaetz**. Yes. May I comment on that, Mr. Chairman?

Mr. **Gibbons**. Yes.

Mr. **Lawaetz**. I believe the real problem started with the rum plant in Puerto Rico. It was dumping a much larger quantity of effluent into an enclosed bay, so the EPA made them put up a treatment plant to take care of that problem. On St. Croix, we are talking about a much smaller amount of effluent that is being dumped out into the open sea that is rapidly dispersed by a strong current that goes by the island, and every marine biologist I have heard testify on this subject has stated it is nontoxic. In fact, many argue it is beneficial.

The main problem, like in Puerto Rico, is one of turbidity, not because of chemical toxicity, but because the EPA had made a requirement for the plant in Puerto Rico. They felt obliged to impose the same requirement on the plant in Virgin Islands, although the conditions were totally different.

Mr. **Gibbons**. As I remember the geography of that area, I think the sea goes down to 12,000 feet not far from there, and I imagine it could absorb any little rum runoff. Those are the kinds of ridiculous things that make us doubt that. I will assist Mr. de Lugo in looking into that one personally, because it doesn't make any sense. Perhaps working together we can get something done about that.

On page 3, item 5, you talk about the excise tax, and you say the excise tax which is collected on gasoline should be returned to us, just as the excise tax collected on rum is presently returned to us. I didn't know that much about the excise tax on gasoline there. We don't return that tax to you now?

Mr. **Lawaetz**. No, sir. When the Organic Act was written, I don't believe anyone visualized a petroleum refinery being placed in the Virgin Islands, and therefore the language was not clear as to how petroleum products would be handled. The language is somewhat vague, in that it stipulates that excise taxes collected on products produced in the Virgin Islands would be returned to the Virgin Islands. I think the Treasury Department has taken exception to technical aspects of the petroleum industry to exclude the return of excise taxes on petroleum products from being returned to us.

What we really seek would be some congressional language to clarify the intent of Congress.

Mr. **Gibbons**. That would be a huge amount of money, would it not?

Mr. **Lawaetz**. I believe it runs about $50 million a year, but if in the clarification of the language the Congress chose not to return all of the tax to us, at least if we had a portion of it on which we could plan our future—as it is now, every major undertaking we go through, like right now the airport in St. Thomas, we have just as urgent a need in St. Croix to extend our runway to 10,000 feet. We have problems with new hospitals, building new schools. We need a funding source for a development bank to continue the development of the island. We do not have funding sources for any of these items.

When I was a boy going to school in St. Croix, the population of the island was about 13,000. Right now it is officially about 49,000, and I think it is more like 60,000. That is on St. Croix alone. We have quadrupled in about 20 years. It has created tremendous strains on our water and power production and distribution systems, and our sewage plants, our roads, all the way down the line, and we are running a catchup game, and we do not have the economic resources to do that catching up.

If these taxes were returned to us, even if there were stipulations placed that it could only be used for capital development projects or for funding the development bank, it would give us a financial footing on which we could plan our future.

Mr. GIBBONS. How much revenue have the Virgin Islands been getting from income tax sources from Hess' operation? They filed a 1981 return in which they had no rebate on the tax. I know the mirror image, how it works. Did you lose a lot of money on Hess? What I am wondering is, why they lost money in 1981.

Mr. WILLIAMS. We are told, Mr. Chairman, that the problem has been one of the downturn internationally of the oil industry with regard to a major oil glut that exists internationally. I see that the director of the Bureau of Internal Revenue is here at the table, and he will be able to address that.

Mr. GIBBONS. What I am interested in, was there some change we made in the income tax law that took them off of the tax roll, or was it a turndown in business? Have they discussed that with you?

STATEMENT OF LEROY A. QUINN, DIRECTOR, BUREAU OF INTERNAL REVENUE, U.S. VIRGIN ISLANDS

Mr. QUINN. Mr. Chairman, my name is LeRoy Quinn. I am the director of the Bureau of Internal Revenue. Hess formerly enjoyed certain exemptions and subsidies under an agreement between the Government and Hess. Recently, the agreement was renegotiated and the Government now enjoys 100 percent of the income taxes Hess would normally pay. However, because of the oil glut and certain other conditions in the oil industry, Hess has not shown any income for the 1981 calendar year, but in the past, under the subsidy program, the Government got as much as $10 million or $12 million a year as their portion of the income taxes.

Mr. GIBBONS. But they attribute the failure to pay taxes to the oil glut and not to some change we made in the tax laws here in the Congress last year. Is that right?

Mr. QUINN. That is correct.

Mr. GIBBONS. I was wondering whether it might have been accelerated depreciation or something of that sort which took them off the tax rolls.

Mr. QUINN. Any future development would be subject to the accelerated depreciation investment credit, but it did not apply in the present structure.

Mr. GIBBONS. They didn't buy tax credits from anyone, did they?

Mr. QUINN. No, they haven't bought tax credits from anyone.

Mr. GIBBONS. Well, I will be happy to work with your people to see if we can't do something to make this bill more attractive to you. I understand you have problems with it, and I don't know whether we want to go to the extent of trying to set up a complicated system to save the jobs of 100 people. I realize 100 people in your small economy are important, and it is very important revenue to your State and local government there, but I don't know. We may get into more trouble with a quota system than we do with that, but there must be some way out of all of this, and we will remain in consideration and consultation over it.

I appreciate your having come this long way to this unhospitable climate. Like you, I left Florida yesterday, and I got a shock when I got off the airplane here. I hope the remainder of your stay in Washington will be pleasant, and I hope when you come back again you won't have this to complain about, not the weather, but this piece of legislation.

With that, we will close the hearing for today, and we will resume tomorrow in this same room at 9:30 with additional witnesses from the private sector, and I guess the members from Puerto Rico are coming in the day after that. Is that right? We have more people from your island tomorrow.

Thank you very much.

[Whereupon, at 6:15 p.m., the subcommittee was adjourned, to reconvene at 9:30 a.m., Wednesday, March 24, 1982.]

CARIBBEAN BASIN INITIATIVE

WEDNESDAY, MARCH 24, 1982.

U.S. House of Representatives,
Committee on Ways and Means,
Subcommittee on Trade,
Washington, D.C.

The subcommittee met, at 9:40 a.m., pursuant to notice, in room 1100, Longworth House Office Building, Hon. Sam M. Gibbons (chairman of the subcommittee) presiding.

Chairman Gibbons. Good morning, ladies and gentlemen. The hearing will come to order.

Today we continue testimony from the private sector on the administration's proposed Caribbean Basin Initiative. We have a large number of witnesses today. We will be finishing tomorrow in room 2203 in the Rayburn House Building. All the witnesses should understand that their statements will be printed in full in the hearing record.

Our first witness today is our colleague from California, Mr. Tony Coelho. I wonder if he would come forward, please.

STATEMENT OF HON. TONY COELHO, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Mr. Coelho. Thank you, Mr. Chairman. I appreciate this opportunity to appear before your subcommittee to discuss the agriculture trade aspects of the Caribbean Basin Initiative.

All of us in Congress have observed a mood in the United States this year. That mood is to force U.S. trading partners to open up their markets for more U.S. agricultural imports. Numerous reciprocity bills reflecting this view have been introduced in both the House and the Senate.

Now, just last Friday, the U.S. Trade Representative announced that 48 new products will be eligible under the generalized system of preferences [GSP] for duty-free shipments into the United States, effective March 31. Over half of these additions were requested by Caribbean countries.

Mr. Chairman, I represent the central part of the San Joaquin Valley in California. In my congressional district alone, there are over 220 commercial agricultural products grown annually. As you can see, I represent a major agriculture producing area in the United States and I am one who appreciates the importance of two-way trading with our international trade partners.

I have serious concerns about the administration's Caribbean policy that I feel need to be carefully addressed by this subcommittee in terms of how this policy will affect U.S. agriculture trade in other parts of the world.

The United States has no overall agricultural trade policy that encompasses both exports and imports. The result is conflicting policies in various parts of the world.

Let me give you a specific example. What the administration is proposing for the Caribbean Basin is very similar to an action that the European Economic Community the [EEC], undertook 12 years ago in the Mediterranean Basin for citrus. When the Europeans requested a waiver under the General Agreement on Trade and Tariffs [GATT], the United States stopped it. Now, 12 years later, the United States must go before GATT and request a waiver for its Caribbean trade policies. No one knows what the outcome will be.

What is known is that we in the United States are closing our eyes to conflicting U.S. trade policies in other parts of the world. We must ask the question, What effect will the Caribbean Basin Initiative have on our ongoing efforts to expand U.S. agriculture exports to the EEC and to Japan, our major agriculture trading partners?

I am afraid that when our Government presses pending 301 trade cases that are now before GATT against the EEC the EEC will point out that the U.S. policy in the Caribbean is in violation of GATT. The United States cannot talk out of both sides of its mouth when it comes to international agriculture trade issues. We must be consistent.

It is my view that Congress has the responsibility to put together a Caribbean Basin Initiative [CBI] that makes sense. For this reason, Mr. Chairman, I am proposing two amendments to the CBI which I hope this subcommittee will consider and accept during its consideration of the President's legislation. Copies of my proposed changes are attached at the conclusion of my printed statement for your easy reference.

My first proposal requires Caribbean countries that export agriculture products into the United States duty free to extend the same preferential treatment duty-free status to any U.S. agriculture products and agricultural byproducts, including wine, that are imported into that Caribbean country.

The second proposal changes the existing GSP program. The centerpiece of the Caribbean Basin Economic Recovery Act is the offer of one-way free trade for virtually all imports from the Basin during a 12-year period. The beneficiary countries, having largely agricultural economies, are expected to benefit particularly from zero-duty treatment on a full range of agricultural articles.

However, this trade arrangement may have limited effect, unless changes are made in the existing program. Every year large numbers of existing agricultural products are designated as eligible articles under GSP. If this practice continues, the competitive advantage recently proposed for the Basin countries will be offset by the benefits accruing to GSP-eligible nations, many of which have more developed agricultural sectors.

One way to prevent this from happening is by prohibiting any further expansion of GSP eligibility for agriculture commodities. By 1985, as export capabilities begin to develop in the Caribbean Basin, GSP treatment currently being granted to agricultural products would be terminated to allow Caribbean countries to receive the full benefit of free trade for the remainder of the 12-year period.

My proposal is consistent with the statutory intent of the GSP program. In proposing the GSP, the drafters intended to assist lesser developed countries in expanding their industries by insuring access to U.S. markets. The GSP list was meant to contain manufactured and semimanufactured items. Only in exceptional circumstances was it to include agricultural and primary products.

This distinction was made with the understanding that many, if not most, developing countries are already competitive in the developed country markets with respect to agriculture and primary products. These countries do not need the preferential duty treatment on agricultural items afforded them through the GSP.

The executive branch has basically ignored this intended distinction, by effectively legislating its own program of indiscriminate eligibility for agricultural products. By terminating the GSP eligibility for such products, we will eliminate the abuse so the program will more accurately reflect its intended purpose.

Mr. Chairman, I want to thank the subcommittee for hearing my proposals today regarding the trade aspects of the Caribbean Basin Initiative. I hope this subcommittee will give serious consideration to these amendments as part of the Caribbean Basin Economic Recovery Act. At this time I am pleased to answer any questions regarding my proposals.

Thank you. I will be glad to pursue these opportunities at the appropriate time.

[An attachment to the prepared statement follows:]

PROPOSED AMENDMENTS TO DRAFT OF THE CARIBBEAN BASIN ECONOMIC RECOVERY ACT OFFERED BY MR. COELHO

Insert the following new paragraph after paragraph (4) of section 102(b):

(5) Unless such country extends duty-free treatment to agricultural products and agricultural byproducts (including wine) that are the growth or manufacture of the United States.

After section 105 insert the following new section:

SECTION 106. GSP TREATMENT REGARDING AGRICULTURAL PRODUCTS AND BYPRODUCTS

After April 1, 1982, no additional agricultural products or byproducts may be designated under section 503 of the Trade Act of 1974 (19 U.S.C. 2463) as eligible articles for purposes of the Generalized System of Preferences. If duty-free treatment under the Generalized System of Preferences is extended beyond January 2, 1985, no agricultural product or agricultural byproduct may be designated under such section 503 after such date as an eligible article.

Chairman GIBBONS. I appreciate the fact that you came here.

We have had some discussion from the Virgin Islands and Puerto Rico and we are going to have more in the next 2 days. Do you have any idea who would be most affected, outside the United States of course, by your proposal to limit duty-free treatment to the recognized nations of the Caribbean Basin? I am just not that familiar with our trade in agricultural products.

Mr. COELHO. What do you mean by "affected," Mr. Chairman?

Chairman GIBBONS. Well, if you deny GSP treatment to other people, who would be the ones that are impacted by the denial?

Mr. COELHO. I could not answer that. I will be glad to submit that for the record, though.

[The following was subsequently received:]

CONGRESS OF THE UNITED STATES,
HOUSE OF REPRESENTATIVES,
Washington, D.C. March 30, 1982.

Hon. SAM M. GIBBONS,
Chairman, Trade Subcommittee,
House Ways and Means Committee, 233 Cannon HOB, Washington, D.C. 20515

DEAR MR. CHAIRMAN: This is to follow-up my March 24 appearance before the Trade Subcommittee, regarding the Caribbean Basin Initiative.

At the conclusion of my comments you asked me which countries would be most adversely impacted by my proposal to limit GSP duty-free treatment to Caribbean nations after January 1985.

According to a GAO Report on GSP, dated November 6, 1980, the five largest exporters of duty-free agriculture goods to the United States are: Taiwan, Korea, Hong Kong, Brazil and Mexico.

I attempted to get a complete GSP country list broken down according to the volume of duty-free agriculture goods shipped to the United States from the U.S. Trade Representative's Office. However, I was informed that their computer will not be programmed to retrieve this type of data until late this summer.

I hope this information is helpful to you. I am available to discuss any portions of my proposal with you, other members of the subcommittee or staff at any time.

Sincerely,

TONY COELHO, *Member of Congress.*

Chairman GIBBONS. All right. Well, I know it is difficult. We will find that out. That is very good question.

Mr. COELHO. You were on the committee, Mr. Chairman, when the bill was drafted and you knew the intent of that section. And if you remember, at that particular time Mr. Strauss was involved and he came to the California delegation and did a lob of lobbying for agriculture. And Bob discussed with us that was not the intent.

And what has happened in effect is that the administration, the last one and this one both, have totally ignored what the intent was of this committee and have just gone ahead and provided a basic loophole here that I do not think was ever intended. It is not reciprocal, and supporting basically the country that it is supposedly trying to help out.

Mr. BAILEY. Thank you, Mr. Chairman.

Congressman, I think part of the problems we have had, at least that I have had, on this Caribbean Basin Initiative is its lack of comprehensive appreciation of American trade policy or domestic difficulties, including security of supply, domestic production, and domestic policy.

We have got recommendations, for example, from the administration that involve changes with investment tax credit policy here in the United States and I do not see how they could accommodate those changes to the Caribbean Basin Initiative. They want to make changes in this country that will emasculate the impact of the existence of the investment tax credit and they want to write it into the CBI.

I want to compliment you for bringing to the attention of the subcommittee some of the problems, for example, with agriculture. We are just not taking an overall view of diplomatic, military, and political implications that impact on American supply and American business decisions. We are also not looking at the transshipment problem properly.

We also have no idea of what kind of security of supply we are going to have, especially in the food area. I know what a champion you have been for building the American wine industry; years and years, and billions of dollars of investment by American producers and producers in all aspects of marketing that this county has undergone.

And yet, I do not think we are appreciating the kind of reciprocal arrangements— I hesitate to use that work, Mr. Chairman; the pun was unintended—for the Caribbean Basin Initiative.

I appreciate your raising these questions. The Chairman is far more knowledgeable in this area than I am. I appreciate your bringing this to our attention.

Mr. COELHO. I think you raise some good points. I just want to reiterate one thing you said. I happen to be one who believes that we need to be doing something in the Caribbean Basin. But I happen to feel that this initiative is not well thought out.

My concern is that we do not have an overall trade policy, and the chairman of this subcommittee has been one of those who is a strong advocate in this area. And I would think before the administration does something on CBI that they should try to decide what their overall trade policy is.

I pointed out in my statement the fact that we are in effect advocating something that we have fought in the past, and we are going to have to get an exemption from the GATT treaty in order to do what we are doing here. That does not make any sense, and I do not really think that the things we do in the area of trade are well thought out in terms of an the overall policy, as you point out, in all different kinds of sectors.

But I just think this whole question of trade is critical to us. It is hurting us in a lot of ways, and the reason it is hurting us is because we do not think the whole thing through. And it is time that we make a major initiative.

I have sent a letter to the President urging him to come forth with a national trade policy. I know that it is under consideration at the White House and I would hope that they would come forth with one, and then we can consider this as part of that. But before that I think we should just hold up and let us put the whole thing together.

I think the concerns of Puerto Rico and the Virgin Islands are very well thought out and things that we should be concerned about. We should not destroy those areas to help out another area. That does not make any sense. That is not what trade is for.

But I appreciate your comments very much.

Mr. BAILEY. Thank you, Mr. Chairman.

Chairman GIBBONS. Thank you, sir.

Mr. COELHO. I thank you, Mr. Chairman.

Chairman GIBBONS. Our next witness is from Schenley Industries, Mr. Frederick O. Petelenz.

STATEMENT OF FREDERICK O. PETELENZ, EXECUTIVE VICE PRESIDENT, SCHENLEY AFFILIATED BRANDS CORP., ACCOMPANIED BY MILTON B. SEASONWEIN, SECRETARY AND GENERAL RESIDENT COUNSEL, SCHENLEY INDUSTRIES, INC.; AND JAY R. KRAEMER, COUNSEL

Mr. **Petelenz**. I would like to thank the committee for the opportunity to appear before you. I would also like to introduce Mr. Seasonwein, resident counsel for Schenley, and Mr. Jay Kraemer.

Chairman **Gibbons**. Thank you. I wonder if you could pull the microphones as close to you as possible. We are having some trouble with the electrical system down here and the reporter is having trouble picking everybody up.

Mr. **Petelenz**. In the interest of moving this thing along, as you requested earlier, Mr. Chairman, I am going to summarize my remarks and take advantage of your offer to have my full testimony in the record.

My name is Frederick O. Petelenz and I am executive vice president of Schenley Affiliated Brands Corp. This is the marketing subsidiary of Schenley Industries, Inc. Schenley manufactures and markets alcoholic beverages and owns a U.S. Virgin Islands corporation, Virgin Islands Rum Industries, Ltd., going under the name of VIRIL. VIRIL operates a rum distillery on St. Croix.

Schenley is concerned over the impact that elimination of the tariff on Caribbean Basin rum would have on VIRIL and the U.S. Virgin Islands. While Schenley and VIRIL do not desire to frustrate the laudable intentions behind the administration's Caribbean Basin Initiative, Schenley and VIRIL are highly distressed by the near-term prospect of a precipitous fall in the U.S. tariff on rums from Caribbean nations, from the current $1.62 per proof gallon to zero.

Because of its willingness to bear its share of increased competition, Schenley did not actively earlier oppose the tariff reductions under GATT. However, Schenley cannot sit silently by and watch the implementation of a policy which targets VIRIL for particularized injury.

More than 85 percent of VIRIL's rum shipped to the United States is transported unaged and in bulk. The rum is either then bottled and marketed under numerous labels that are priced well below that of well-known aged brand-name rums or is used in premixed cocktails.

This unaged bulk product sold by VIRIL is in the nature of a commodity and is in stark contrast to rums produced in Puerto Rico, which are subject to an aging requirement under local law and are then marketed by their producers and affiliates under brand names, such as Bacardi and Ronrico.

The demand for bulk, unaged rum from the Virgin Islands is extremely price sensitive. If the Virgin Islands rum ceases to be less expensive than rum from other Caribbean sources, purchasers of Virgin Islands rum will rapidly turn to other rum producers.

The threat to VIRIL's U.S. market is real. These producers stand ready to take immediate advantage of any tariff elimination. VIRIL's economic well-being is a key factor in the continuing economic and social development of the U.S. Virgin Islands. VIRIL is the source of about 95 percent of the Virgin Islands rum sold in the United States. The Virgin Islands rum industry provides about 100 jobs, equivalent to 3 percent of the total manufacturing employment in the Virgin Islands.

Excise taxes collected in the United States on the sale of Virgin Islands rum are, after subtracting collection costs, rebated to the government of the Virgin Islands. They provide a vital source of the government's revenue, representing nearly 20 percent of the annual gross revenues of the Virgin Islands government.

The Caribbean Basin Initiative as proposed by the administration would harm the Virgin Islands rum industry and inevitably lead to lost jobs, as well as reduced revenues to the local government. Under present conditions, elimination of the rum tariff would lead U.S. purchasers of Virgin Islands rum to turn to alternative rum suppliers in the non-U.S. Caribbean.

Since many other Caribbean countries already have lower wage rates, have molasses locally available, may transport goods in non-U.S. vessels and do not impose substantial environmental and other regulatory burdens now applicable in the Virgin Islands, the competitive position of rum production in the Virgin Islands would clearly be adversely affected.

The administration recognizes that the proposed elimination of the tariff is likely to cause significant harm to the Virgin Islands and the rum industry there. The administration proposes to offset the anticipated revenue loss to the Virgin Islands government, but has made no provision to ameliorate the increased competitive burden placed on VIRIL.

VIRIL's efforts to expand its export market have been blocked by effective exclusion from major non-U.S. markets. The EEC, for example, allows rum from many Caribbean nations to be imported duty free, subject to certain quota levels. Since the Virgin Islands is a U.S. possession, rum from the Virgin Islands is not afforded such duty-free treatment. With the market for unaged bulk rum so sensitive to price, the Virgin Islands is thus effectively foreclosed from competing in European markets.

Similarly, while a high tariff keeps Virgin Islands rum out of Canada, the Commonwealth countries of the Caribbean have long enjoyed preferential access to the Canadian rum market.

The lifting of U.S. tariffs on Caribbean rum would enable most foreign Caribbean rum producers to export duty free to European, Canadian, and United States markets, while VIRIL would effectively remain shut out of all but the last and with greatly reduced capacity to compete effectively even at home.

The administration's proposal makes little sense when it comes to Virgin Islands rum. Compare the minimal benefit that this policy will produce on other Caribbean islands to the harm visited on the workers and people of the Virgin Islands and the Virgin Islands government.

Since the most probable response to the elimination of the U.S. tariff on rum would be the expansion of rum production by existing facilities in the Caribbean Basin rather than the construction of new facilities, the extent to which additional rum operations will spur the economies of the Caribbean Basin countries is limited at best. This benefit, when weighed against the damages that would be caused to the Virgin Islands by the implementation of the administration's rum tariff proposal, demonstrates the lack of wisdom behind that proposal.

The supposed safeguard mechanism of the CBI is cumbersome and unwieldy. We understand that past efforts in utilizing sections 201 and 203 of the Trade Act of 1974 demonstrate that a domestic petitioner must meet a very heavy burden of proof, and even if the International Trade Commission finds in the petitioner's behalf, relief is still in the President's discretion. By the time VIRIL could present its case to the ITC and persuade the Government that relief should be granted, VIRIL's markets could be lost.

Schenley and VIRIL strongly support maintaining the existing tariff on rum. If the Congress in its wisdom determines that some tariff relief to foreign Caribbean rums is necessary and appropriate, there are ways to give such relief which would be less devastating to VIRIL than the administration's sweeping proposal.

Schenley's suggestions are intended to enable VIRIL to remain competitive while at the same time opening the U.S. market to duty-free entry for foreign Caribbean rum on a substantial and expanding basis. One idea is to give the President authority to remove the tariff on bottled rum but not on bulk rum. This would maximize the new jobs in beneficiary countries without sacrificing the most vulnerable segment of the domestic rum industry.

The other concept has two aspects, both of which are equally important: First, VIRIL needs regulatory relief under the Clean Water Act if it is to stand any chance at all of competing effectively with bulk rum producers elsewhere in the Caribbean. Without some concrete assurance that the regulatory burden imposed on VIRIL with respect to the discharge of the distillery waste—incidentally, a burden that is pointless as far as water quality interests are concerned—would be removed, VIRIL's continuing efforts to compete in price-sensitive markets would be further jeopardized.

The second aspect of this concept involves tariff-free quotas and trade reciprocity. If the Congress decides to permit the tariff on bulk rum to be eliminated, this should occur in conjunction with a provision authorizing the President to grant to each qualifying basin country an annual duty-free quota of up to 110 percent of the historical high levels of rum entering U.S. trade channels.

Furthermore, in the name of equal treatment, Schenley would not oppose a regime under which the tariff-free entry quotas of foreign Caribbean rums were increased above 110 percent from year to year, so long as: (A) total Virgin Islands rum sales to the United States, its CBI partners, and EEC countries do not fall below 95 percent of their 1981 levels; and (B) Virgin Islands rum had access to European, Canadian, Mexican, Colombian, and Venezuelan markets on terms and conditions no less favorable than those applicable to rum from the country seeking a duty-free quota from the United States higher than 110 percent.

In both the areas of regulatory relief and trade reciprocity, all Schenley and VIRIL seek is the chance to compete with the foreign producers on equal terms in all the markets open to them, and free of undue and unnecessary regulatory burdens which they do not bear. We are prepared to make more than our share of the sacrifices necessary to spread prosperity to other neighboring countries throughout the Caribbean Basin. VIRIL is prepared to compete with foreign producers in the United States and other markets and is confident that, given an equal chance, VIRIL can do so successfully.

Unless modifications are made to reduce the adverse impacts on Virgin Islands rum, and unless regulatory relief vis-a-vis environmental requirements is soon forthcoming, the CBI will deliver to the people of the region a most unfortunate message about U.S. treatment of those who rely on this country for their economic well-being.

Thank you very much.

[The prepared statement follows:]

STATEMENT OF FREDERICK O. PETELENZ, EXECUTIVE VICE PRESIDENT, SCHENLEY AFFILIATED BRANDS CORP.

Good morning, Mr. Chairman and members of the Subcommittee. I would like to thank you all for the opportunity to appear before you. My name is Frederick O. Petelenz, and I am Executive Vice President of Schenley Affiliated Brands Corp., the marketing subsidiary of Schenley Industries, Inc. As you may know, Schenley manufactures and markets alcoholic beverages. Schenley owns a U.S. Virgin Islands corporation, Virgin Islands Rum Industries, Ltd. -- known by its acronym "VIRIL" -- which operates a distillery on St. Croix. The competitive viability of VIRIL is inextricably tied up in the matters before you today.

I have come here to express our concern over the impact that elimination of the tariff on Caribbean Basin rum would have on VIRIL and the United States Virgin Islands. While Schenley and VIRIL do not desire to frustrate the laudable intentions behind the Administration's Caribbean Basin Initiative, we are highly distressed by the near-term prospect of a precipitous fall in the U.S. tariff on rums from Caribbean nations, from the current $1.62 per proof gallon to zero. As a matter of historical perspective, I would note that we took no active role in 1977 to oppose gradual unilateral rum tariff reductions under the GATT. That set of reductions would have dropped the tariff from $1.75 to $1.40 per proof gallon by 1987.

Our previous restraint with respect to earlier, more moderate tariff reductions has demonstrated our willingness to bear our share of increased foreign competition. However, we cannot sit silently by and watch the implementation of a policy which targets VIRIL for particularized injury.

To fully explain the impact that the elimination of the rum tariff will have on VIRIL and the Virgin Islands, I must briefly describe VIRIL's operations and the significance of those operations to the Virgin Islands economy. More than 85% of VIRIL's rum shipped to the United States is transported unaged and in bulk. The rum is then either bottled and marketed under numerous labels at a price well below that of well-known aged, brand name rums or is used in pre-mixed cocktails. This unaged bulk product sold by VIRIL, which is in the nature of a commodity, is in stark contrast to rums produced in Puerto Rico (which are subject to an ageing requirement under local law, and are then marketed by their producers' affiliates under brand names, such as Bacardi or Ronrico).

The demand for bulk, unaged rum from the Virgin Islands is, both absolutely and in comparison to Puerto Rican rums, extremely price-sensitive. Since the initial purchasers of Virgin Islands rum are largely businessmen highly conscious of the price of goods in their inventory, we expect that they will rapidly turn to other rum producers if Virgin Islands rum ceases to be less expensive than rum from other Caribbean sources. And make no mistake, Caribbean rum producers, some of them the very same companies with rum distilleries or rum-producing affiliates in Puerto Rico,*/ are ready to take immediate advantage of tariff elimination. In recent years, over 85% of the foreign rums entering U.S. trade channels have come from Caribbean Basin countries, 65-75% of the total from Jamaica alone.

To understand why damage to VIRIL translates to harm to the Virgin Islands, a few facts and figures must be recognized. VIRIL is the source of about 95% of the V.I. rum sold in the U.S. The V.I. rum industry provides about one hundred jobs, equivalent to three percent of the total manufacturing employment in the Virgin Islands. Excise taxes collected in the United States on the sale of Virgin Islands rum are, after subtracting collection costs, rebated to the Government of the Virgin Islands. Excise tax rebates currently represent nearly twenty percent of the annual gross revenues of the Virgin Islands Government. VIRIL's economic well-being is thus a key factor in the continuing economic and social development of the Virgin Islands.

As noted above, under present conditions, elimination of the rum tariff would lead U.S. purchasers of Virgin Islands rum to turn to alternative rum suppliers in the non-U.S. Caribbean. Since many other Caribbean countries already have lower wage rates, have molasses locally available, may transport goods in non-U.S. vessels, and do not impose the substantial environmental and other regulatory burdens now applicable in the Virgin Islands, the competitive position of rum production in the Virgin Islands would clearly be adversely affected. Schenley wants to see the economy of the Virgin Islands continue to grow and prosper. However, without a substantial U.S. tariff on foreign rum, and in light of the present competitive disadvantages I have just listed, expanding or, I am afraid, even maintaining a rum distillery there is brought into serious question.

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*/ Seagram, which owns Puerto Rico Distillers, Inc., also owns the Myers Rum distillery in Jamaica. Bacardi has distilleries on Martinique and in the Bahamas. Even the small Brugal distillery on St. Croix, which now produces for the U.S. market, might be replaced by production from Brugal's distillery in the Dominican Republic.

The Administration recognizes that the proposed elimination of the tariff on rum is likely to cause significant harm to the Virgin Islands and to the rum industry there. In the Fact Sheet accompanying President Reagan's Caribbean Basin Policy address of February 24, the likelihood of harm to U.S. rum distillers' sales is expressly recognized. The Fact Sheet states:

> -- Inclusion of rum in the proposed Free Trade Area is coupled with a proviso that excise taxes on imported rum will be rebated to Puerto Rico and the U.S. Virgin Islands.

Thus, the Administration proposes to offset the anticipated revenue loss to the Virgin Islands Government, but has made no provision to ameliorate the increased competitive burden placed on VIRIL. This was expressly recognized by Mr. Ballentine of the Treasury Department in response to a question posed by this Subcommittee during the hearing last Wednesday.

You may wonder why VIRIL doesn't respond to the threat of the elimination of U.S. rum tariffs by seeking to develop a broader export market. After all, other people in the world besides Americans drink rum. Unfortunately, however, VIRIL has been effectively excluded from the non-U.S. rum market. The EEC, for example, allows rum from many Caribbean nations to be imported duty-free, subject to certain quota levels. Since the Virgin Islands is a U.S. possession, however, rum from the Virgin Islands is not afforded such duty-free treatment. With the market for unaged bulk rum so sensitive to price, the Virgin Islands is thus effectively foreclosed from competing in European markets. Similarly, while a high tariff keeps Virgin Islands rum out of Canada, the Commonwealth countries of the Caribbean have long enjoyed preferential access to the Canadian rum market.

The lifting of U.S. tariffs on Caribbean bulk rum would have serious competitive consequences. While most foreign Caribbean rum producers would be able to export rum duty-free to European, Canadian, and United States markets, VIRIL would remain effectively shut out of all but the last and with greatly reduced capacity to compete effectively even at home. Caribbean bulk rum made at lower cost on neighboring islands would replace an increasing amount of Virgin Islands rum in the United States, and Virgin Islands rum would continue to be subject to prohibitive tariffs levied by the EEC countries and Canada. The same situation would probably prevail as to markets in Mexico, Colombia, and Venezuela, with whom the U.S. is cooperating in the CBI.

It is important to recognize that the Administration's proposals simply make no sense when it comes to Virgin Islands rum. Compare the overall benefit that this policy will produce on other Caribbean islands to the harm visited on the workers and people of the Virgin Islands and the V.I. Government. It is not likely that new rum distilleries will be built or new workers employed in Caribbean Basin countries. More probable is the scenario in which existing distilleries in the Caribbean Basin (some of which are owned by multinational corporations*/ headquartered outside the Caribbean), would simply expand their production by operating more days per year. Therefore, the extent to which additional rum operations will spur the economies of Caribbean Basin countries is limited at best. This benefit, when weighed against the damage which will be caused in the Virgin Islands by the implementation of the Administration's rum tariff proposal, demonstrates the lack of wisdom behind that proposal. It is simply illogical to jeopardize a vital sector of the economy of the Virgin Islands in return for such a small potential benefit among CBI beneficiary countries.

Let me speak just briefly on the supposed safeguard mechanism in the CBI in instances of injury to domestic industry -- resort to the International Trade Commission. The analogue of this mechanism now embodied in Sections 201 and 203 of the Trade Act of 1974 has proven a cumbersome and unwieldy device indeed. When invoked, it demands a very heavy burden of proof on the part of the domestic petitioner and, even if the ITC finds in the petitioner's behalf, relief is still in the President's discretion. Accordingly, the mechanism proposed by the Administration is far too time-consuming, expensive, and uncertain a route to relief to assuage our concerns. By the time we could present our case to the ITC and persuade the President that relief should be granted (even assuming the latter did not conflict with Executive Branch policy concerns -- regarding Jamaica, for example), our markets could be lost irreversably.

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*/ E.g., Myers rum of Jamaica is owned by Seagram, a Canadian corporation; Pott rum of St. Maarten is owned by a German corporation.

Thus far, I have told you why we think immediate removal of the tariff on foreign Caribbean rum is not a sound policy. I want to make crystal clear VIRIL's position that the existing tariff on rum should be maintained. But if the Congress, in its wisdom, determines that some tariff relief for foreign Caribbean rums is necessary and appropriate, there are ways to structure such relief which would be less devastating to VIRIL than the Administration's sweeping proposal.

One such relief mechanism would be to authorize the President to remove the tariff on rum imported into the U.S. in bottles (i.e. TSUS 169.13), but retain the tariff on rum in bulk containers (i.e. TSUS 169.14). This regime would preserve a price advantage for domestic bulk rum, the most vulnerable and price-sensitive segment of the domestic rum industry. At the same time, it would encourage Caribbean Basin rum producers to expand and concentrate their operations in bottled rum. Since bottling is the most labor intensive phase of rum production, such a regime would also maximize the number of new jobs created in the beneficiary countries.

Let me also explain an alternative concept we believe might enable VIRIL to remain competitive while at the same time opening the U.S. market to duty-free entry of foreign Caribbean rum, both bulk and bottled, on a substantial and expanding basis. There are two aspects to this concept and both are of equal importance -- to implement one without the other would still, in all probability, leave VIRIL with a materially weakened competitive position.

The first aspect is, unfortunately, not within the direct jurisdiction of the Ways and Means Committee. I will, therefore, address it only briefly here. VIRIL needs regulatory relief under the Clean Water Act if it is to stand any chance of competing effectively with bulk rum producers elsewhere in the Caribbean. Were it not for a Request for Reconsideration filed with the Environmental Protection Agency last year, VIRIL would at this very time either be shut down or engaged in building a $4 million waste treatment plant.*/ Operating costs of the treatment facility, if built, would mean hundreds of thousands of dollars each year in addition.

This is far and away VIRIL's greatest regulatory burden, and it is one our foreign competitors do not face, though they discharge their distillery wastes into the very same body of water. Even without a tariff reduction, this regulatory requirement, pointless as far as water quality interests are concerned, severely jeopardizes VIRIL's capacity to compete successfully in a price-sensitive market.

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*/ As a point of reference, you should know that $4 million exceeds the current book value of all of VIRIL's present fixed assets.

As noted, we have sought regulatory relief by administrative ruling from the EPA. As Mr. Sanjuan testified last Wednesday, the Interior Department supports administrative flexibility in this regard. We also hope that legislation will be introduced as part of the CBI package which would exempt certain dischargers in the Virgin Islands from the most stringent aspects of the Clean Water Act (i.e., those aspects not suited to the Territory's climatic, geographic, or economic conditions). While I cannot predict what might be the outcome of these efforts, I want to make it clear that VIRIL's capacity to withstand elimination of the tariff is a direct function of regulatory relief to let us compete with foreign producers on a more equal footing.

The second aspect has to do with tariff-free quotas and trade reciprocity. As you know, the free trade area program supported by the Administration contains an exception for the sugar industry. As important as the sugar industry is to the United States, the rum industry is proportionately much more important to the Virgin Islands.

If the Congress decides to permit the tariff on bulk rum to be eliminated, we believe this should occur, as with the large foreign sugar producing countries, in conjunction with a provision authorizing the President to grant to each qualifying Basin country an annual duty-free quota of up to

110% of the historical high levels of rum entering U.S. trade channels.*/ And, in the name of equal treatment, we would go further. There is no reason why foreign producers should not share in a general expansion of the rum markets open to us. We would not oppose a regime under which the tariff-free entry quotas of foreign Caribbean rums were increased above 110% from year to year so long as: (a) total Virgin Islands rum sales to the U.S., its CBI partners, and EEC countries did not fall below 95% of their 1981 levels; and (b) Virgin Islands rums had access to European, Canadian, Mexican, Colombian, and Venezuelan markets on terms and conditions no less favorable than those applicable to rum from the country seeking a duty-free quota from the U.S. higher than 110%. We have discussed the details of such a program with Congressman de Lugo's staff and would be pleased to have similar discussions with the members and staff of this Subcommittee. We are convinced that means exist by which the U.S. rum market can be substantially opened to foreign Caribbean rum producers without irreparably compromising VIRIL's competitive position. All we are asking, and I want to stress this, is the chance to compete with the foreign producers on equal terms in all the markets open to them and free of undue and unnecessary regulatory burdens which they do not bear.

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*/ Any foreign rum now held in bond in the U.S. on which the tariff has not yet been paid should either be subject to the tariff or counted as part of the quota amount.

Mr. Chairman, Schenley and VIRIL recognize the importance of an economically prosperous Caribbean. We have worked together with the residents of the United States Virgin Islands -- the Americans of the Caribbean -- to help bring prosperity to the area. We are prepared to make more than our share of the sacrifices necessary to spread prosperity to other neighboring countries throughout the Caribbean Basin. All we ask is that the sacrifices be limited to what is reasonable and truly likely to help those countries rather than unnecessarily burdensome and harsh in their consequences. VIRIL is prepared to compete with foreign producers in the U.S. and other markets, and we are confident that, given an equal chance, VIRIL can do so successfully.

We also believe, however, that unless modifications, such as those we have outlined, are made to the Administration's proposal to reduce the adverse impacts on Virgin Islands rum, and regulatory relief vis-a-vis environmental requirements is forthcoming, the CBI will deliver to the people of the Region a most unfortunate message about U.S. treatment of those who rely on this country's policies for their economic well-being. Such a short-sighted approach ill-serves us all. What the Caribbean needs, and the situation with rum is in some respects a microcosm of this, is not a dramatic sweep of the hand, but a carefully thought out trade policy which will enable our neighbors to enjoy a fair share of U.S. markets and, at the same time, open reciprocal trade opportunities in new markets to the U.S. business community established in the Virgin Islands and Puerto Rico.

Thank you very much, Mr. Chairman.

Mr. **Petelenz**. I further understand that you and other members of your committee have scheduled a recess visit to the Virgin Islands.

Chairman **Gibbons**. I wish we had, but the members did not want to go to the Virgin Islands because we would get panned in the press for a junket. And I hate to say that, but that is true. We cannot go to the Virgin Islands. You spend all your time explaining why you went there and nobody cares. So we are going to have to avoid the Virgin Islands for that purpose, and that is a terrible thing to say, but that is part of the system.

Mr. **Petelenz**. I am sorry to hear that.

Chairman **Gibbons**. I am, too. I think it is atrocious. But the Members just do not want to go there, because of the political liability attached to it.

Let me ask you some things, Mr. Petelenz. How many people do you employ in the Virgin Islands in your rum operations?

Mr. **Petelenz**. In our rum operation we have approximately 70 people. In the entire rum industry in the Virgin Islands there are about 100.

Chairman **Gibbons**. Yours is about 70, of 100 in total amount?

Mr. **Petelenz**. Yes.

Chairman **Gibbons**. How long have you been operating there?

Mr. **Petelenz**. The operation has been there since 1936, and Schenley's acquisition was in the fifties.

Chairman **Gibbons**. You import molasses, is that right, from the other islands, and then it goes through the distillation process?

Mr. **Petelenz**. Yes.

Chairman **Gibbons**. And it is all shipped out in bulk, is that right?

Mr. **Petelenz**. All of our production is shipped out in bulk.

Chairman **Gibbons**. Does it have to be aged after it gets to this country?

Mr. **Petelenz**. No, sir.

Chairman **Gibbons**. Not for the mix it goes into?

Mr. **Petelenz**. Well, a lot of it is so sold—there has been a trend in the rum industry to a lighter product with such characteristics of alcoholic beverages, and it is that product, which is what we call generic, that is the most desirable.

In Puerto Rico they age the rum under their local regulations.

Chairman **Gibbons**. And of course, being a U.S. possession you get no duty-free treatment or preferential treatment from the European Community. In fact, you get discriminatory treatment in the European and Canadian market, is that correct?

Mr. **Petelenz**. That is correct.

Chairman **Gibbons**. How much unaged rum is imported into the United States? Do we import any unaged rum into the United States?

Mr. **Petelenz**. Yes, sir. There is a substantial amount coming from Jamaica and that is basically the largest portion of it. We control the most significant percentage from the Virgin Islands.

Chairman **Gibbons**. It all comes out of your distillery there, is that right?

Mr. **Petelenz**. Yes.

Chairman **Gibbons**. Are there any of the other islands of the Caribbean?

Mr. **Petelenz**. No, sir. A lot of the other products come in cases to the United States.

Chairman **Gibbons**. How big is your operation in Jamaica?

Mr. **Petelenz**. We have no operation in Jamaica. We do not do anything there. There is a Seagram affiliate that operates there.

Chairman **Gibbons**. Excuse me, I am sorry.

Do you know anything about the size of their operation? Is it larger than yours or——

Mr. **Petelenz**. Considering the amount of rum coming out of there to the United States, it would not seem to be. But there have been reports and studies made of the capabilities to produce rum in these other Caribbean Basin countries, and their capabilities are greater than their utilization of their equipment. And as I had mentioned earlier, these distilleries just go onstream for a longer period of time.

Chairman **Gibbons**. The effluent was a matter of discussion yesterday, and I guess I am vaguely familiar with your islands down there. I have never been to St. Croix, but I know there is an awful lot of seawater and the sea is very deep in most of that area.

Have you ever had any complaints from the local people about the effluent?

Mr. **Petelenz**. I will refer that question to Mr. Kraemer.

Mr. **Kraemer**. Not to my knowledge, sir, with one exception. There is a discharge from the distillery which goes out offshore about 1800 feet. At one point that discharge line, which is owned by the Virgin Islands, broke, and some of the material washed up back on the shore and there were some complaints at that time.

But to the best of my knowledge that is the extent of it. There have been no complaints in the last several years.

Chairman **Gibbons**. And your plant is on the south shore of the island, is that right? Are there any coves or anything like that?

Mr. **Kraemer**. No, sir. The current takes the effluent about 5 miles down the coast of the island in a westerly direction, and when it reaches a place called Sandy Point, which is the westernmost point of the island, all of it is dispersed. I guess the next landfall of that current would be Venezuela.

Chairman **Gibbons**. Mr. Bailey?

Mr. **Bailey**. Thank you, Mr. Chairman.

First of all, on the effluent, as I understand it it is not really a pollutant item; it is a food source. Am I right about that?

Mr. **Kraemer**. That is essentially correct, sir. I think you could best describe it as molasses without the sugar and with water mixed in. It is, however, under the Clean Water Act presently defined as a pollutant.

Mr. **Bailey**. They have undoubtedly tried to classify agricultural lime as a hazardous substance, too. If you transport it in 5,000 pound loads and dump it in a stream, the lime will change the pH of the water to the point where it kills fish in the immediate vicinity. If you know anything about farming, you know how absurd that point of view is. But somebody sitting at a desk has to justify their existence, I guess.

Let me ask you this. Canada you say does not impose a duty on rum brought in from the Caribbean generally?

Mr. PETELENZ. From the Commonwealth countries.

Mr. BAILEY. From the Commonwealth countries.

Mr. PETELENZ. Yes.

Mr. BAILEY. Is Canada going to change for these countries or is Seagram going to get upset about that? Are they upset about that, or is Canada not going to change that, do you know?

Mr. PETELENZ. Well, one of our points was that we would like them to change that. They are cooperating in the Caribbean Basin Initiative, as I understand.

Mr. BAILEY. They do not do too much up there.

How much investment is going to result from this rum change in the Caribbean Basin outside of Puerto Rico and the Virgin Islands? How many jobs is it going to bring to these Caribbean countries?

Mr. PETELENZ. I do not think it is going to bring very many, Mr. Bailey, because these distilleries are in place today, and a distillery operation as such does not require very many additional workers——

Mr. BAILEY. It is not labor intensive, then?

Mr. PETELENZ [continuing]. To go onstream, or to work a longer number of hours.

Mr. BAILEY. Is it a very low capacity that distilleries have? In other words, how is your capacity geared? Do you run at 100 percent?

Mr. PETELENZ. Well, our capacity is 5 million gallons a year, and we are effectively shipping about 3.5 million. There is always a certain amount of down time with any distillery operation.

Mr. BAILEY. What is their situation like?

Mr. PETELENZ. My feeling is that they are operating at a very low percentage capacity.

Mr. BAILEY. They are not going to increase very many jobs down there, then?

Mr. PETELENZ. No, sir.

Mr. BAILEY. What is the reason? Is it to look good on paper? Do you suspect that there has not been a whole lot of homework done on this?

Mr. PETELENZ. That is basically what we feel, that even as the previous witness indicated, we do not think that this thing has been thought through completely, especially its impact on certain commodities or certain agricultural products, and in this particular case, there is a very special situation in the U.S. Virgin Islands.

Mr. BAILEY. So what you are telling me is that we increased a few jobs down there, but probably not too much more. It will not increase or create new jobs?

Mr. PETELENZ. With our 3.5 million production, and with five or six other distilleries, you can see that we are not affected very much.

Mr. BAILEY. Are there any alcohol byproducts besides alcoholic beverages?

Mr. PETELENZ. No, sir.

Mr. BAILEY. What about Europe? Why do you favor imposing a duty on——

Mr. **Petelenz**. That is because several countries in the Caribbean Basin are members of the EEC, by virtue of being part of the Netherlands and Commonwealth members or the colonies of EEC countries.

Mr. **Bailey**. So the market that is going to be increased is not going to be very much of a world market. We are not talking about increasing a Caribbean Basin capacity, but simply talking about a replacement of capacity here in the United States.

Mr. **Petelenz**. Not unless we get some relief.

Mr. **Bailey**. So you are not going to increase sales to Europe? I mean if we make this change, we are not going to be helping the Caribbean increase their sales to Africa, South America, Indonesia?

Mr. **Petelenz**. No, sir, because they presently have that market.

Mr. **Bailey**. They presently have that market. You say 100 jobs. It might impress me, but it is not going to impress a whole lot of people. What would you do? How would you adjust as a company, and if the worst comes, and this thing passes? What would you do?

Mr. **Petelenz**. Well, the company has several alternatives. We could close down the facility. That is one approach.

Mr. **Bailey**. You have got 100 direct jobs, you have got to have a few more.

Mr. **Petelenz**. We have about 70.

Mr. **Bailey**. So you factor about 30. Where would you go for your rum, then? Do you buy it from somebody else?

Mr. **Petelenz**. Well, we have the opportunity to buy it from Caribbean Basin countries, from other countries in the Caribbean, but we are not talking of our industry so much as we are talking of our customers. We sell to customers of the United States.

Mr. **Bailey**. Is there any difference in quality?

Maybe that is a bad question.

Mr. **Petelenz**. Well, it is a bad question. [Laughter.]

Mr. **Bailey**. Well, I have a lot of questions about this. 10 or 15 years down the road, I want to be able to justify what it means in terms of comprehensiveness. I sympathize with the administration's need and what the countries need, and to try to help us in an innovative way with dealing with world problems; but I do not think the American taxpayers—I just fail to see the justice of an approach like this. It is a silly way to try to attract investment down there. We have American investment in other countries around the world, and politically it has done us very little good, because of the way that we have done it. We are not transferring the real benefits, and it is hard to turn around in this country and contradict where people are going to lose their jobs. It does not solve the structural problems in the United States and those of our people.

I thank you.

Thank you, Mr. Chairman.

Chairman **Gibbons**. Thank you, sir.

Our next group of witnesses is from the Virgin Islands Trade and Economic Development Industries. Peter Hiebert, Joaquin Marquez, and Neil Kimmelfield.

STATEMENT OF PETER N. HIEBERT, TREASURER, AND JOAQUIN A. MARQUEZ, SECRETARY, VIRGIN ISLANDS TRADE AND ECONOMIC DEVELOPMENT INSTITUTE, ACCOMPANIED BY NEIL KIMMELFIELD, COUNSEL

Chairman GIBBONS. All right, gentlemen, you may proceed as you wish.

Mr. HIEBERT. I am Peter Hiebert. On my left is Joaquin Marquez, and on my right is Neil Kimmelfield, our counsel.

Chairman GIBBONS. Get up close to that microphone so we can hear you.

Mr. HIEBERT. We have a statement which we would like to include in the record. For purposes of saving time I would like to summarize our statement.

Mr. Chairman, and members of the House Ways and Means Committee, the Virgin Islands Trade and Economic Development Institute is pleased to have this opportunity to testify regarding H.R. 5900, the administration's proposed Caribbean Basin Economic Recovery Act. The Institute is an independent, nonprofit organization, dedicated to the promotion of economic development and business investment in the U.S. Virgin Islands. The institute's members include both U.S. companies operating in the Virgin Islands, as well as local territorial businesses.

The Virgin Islands Trade Institute supports the stated goals and objectives of the President's Caribbean Basin Initiative and believes that a concerted effort to reduce poverty and misery in that region is long overdue.

However, we believe that progress in the Caribbean Basin must not be allowed to come at the economic expense of the Virgin Islands. Recognizing that the Virgin Islands is part of both the United States and the Caribbean, we believe that such a result ultimately would thwart the purposes of the CBI.

Mr. Chairman, as I mentioned, I would like to summarize our comments and submit the full statement for the record.

The centerpiece of the President's proposal is the establishment of a one-way free trade zone between Caribbean Basin countries and the United States. While the overall effect on the U.S. mainland economy may not be significant, the impact of such a policy on the competitive position of the Virgin Islands could be disastrous.

There are several components to this problem:

First, because Caribbean countries are not subject to U.S. laws, including minimum wages, labor standards, environmental restrictions, occupational, health and safety requirements, and American-flag shipping limitations, as well as other regulatory burdens too numerous to mention here, foreign producers can undercut the price of goods manufactured in the Virgin Islands.

Without a tariff, there is nothing to protect the companies already located or contemplating location in the Virgin Islands.

Second, it must be remembered that the Virgin Islands lies outside of the customs territory of the United States and, unlike Puerto Rico, is essentially considered to be a foreign country for trade purposes.

Thus, Virgin Islands products, unless otherwise exempted, are subject to duty when entering the United States.

Although provisions set forth under general headnote 3(a) provide duty-free treatment under some circumstances, the advantages provided by general headnote 3(a) have eroded over the last 10 years.

While the administration has proposed extending to the Virgin Islands, as an alternative to the general headnote 3(a), the same rules of origin test which it has proposed extending to the other Caribbean Basin countries, such a provision will unfortunately have little benefit for the Virgin Islands. Unlike Jamaica, the Dominican Republic, or the Central American countries of the Caribbean, the Virgin Islands has no natural resources or indigenous materials to use in manufacturing.

Consequently, unlike its Caribbean neighbors which can utilize local materials in meeting the proposed rules of origin test, Virgin Islands products could qualify for duty-free entry under the CBI formula only by adding 25 percent of the appraised value of such products in direct manufacturing or processing of high cost foreign materials.

Quite simply, only the Virgin Islands textile industry would be benefited by this provision. However, textiles are not eligible under the proposed free trade zone.

Third, in order to compete effectively with other Basin countries, the Virgin Islands requires substantial improvements in its infrastructure, including new airport facilities on St. Thomas and major improvements for water and power.

Finally, the proposed elimination of the U.S. tariff on rum imported from CBI beneficiary nations poses a direct threat to both the Virgin Islands rum industry and the fiscal integrity of the Virgin Islands government. The rum industry is presently the Virgin Islands government's largest single source of revenue, generating in 1980 over $35 million in Federal excise taxes. Because these funds are used to meet the general obligations of the territorial government, including the provision of basic services, it is essential that the Virgin Islands rum industry remain healthy and competitive.

Foreign rum producers are not subject to the same heavy environmental, wage, safety and other regulatory burdens, and they can manufacture the same product at lower cost. The present tariff on rum then constitutes the only protection which assures the continued viability of the Virgin Islands rum industry. Removal of this protection without offsetting governmental actions such as those relating to environmental requirements, would probably assure the ultimate demise of the rum industry of the Virgin Islands.

The Virgin Islands Trade and Economic Development Institute proposes the following specific provisions with respect to the free trade provisions of the proposed legislation:

First. Rum should be excluded from the list of articles eligible for duty-free treatment. Because of the excise tax rebates, rum plays an even greater role in the economies of the Virgin Islands and Puerto Rico than do the textile and the sugar industries in the United States.

Second. If Congress in its wisdom decides to eliminate the tariff on rum, we believe that qualifying basin countries should be limited, as in the case of large foreign sugar producing countries, to a duty-free quota of up to 110 percent of historic volumes of rum entering the United States.

Also, we would recommend that the snap-back provision embodied in section 104(b) of H.R. 5900 be amended so that the President will be required to consider compensatory measures, including reimposition of the duty, if the amount of excise taxes covered into either the treasury of the Virgin Islands or Puerto Rico pursuant to section 302 is reduced below the amount which would have been covered over if the imported rum had been produced in such territory.

Third. The United States should take steps to insure that products manufactured in the Virgin Islands, including rum, should be granted access to markets in Canada and the EEC, under conditions no less favorable than products manufactured in CBI beneficiary countries.

Fourth. The safeguard mechanism embodied in sections 103(d) and 104(e) provides inadequate relief. Given the fragility of the Virgin Islands' competitive position, the escape clause provisions of title II of the 1974 Trade Act would fundamentally operate ex post facto. Once the injury is complete and the Virgin Islands industries irreversibly lost, no amount of relief recommended by the International Trade Commission or adopted by the President would be adequate.

The substantial injury test imposed by the 1974 act applies to the entire U.S. domestic industry producing a like or directly competitive article. Because of the obvious size disparities, increased Caribbean Basin imports into the United States could substantially injure or even destroy a competing industry in the Virgin Islands which is dependent upon exports to the United States, while such increased imports would hardly affect the larger U.S. industry. We therefore recommend that section 104(e) be amended to provide that "in determining whether an industry of a U.S. insular possession has been injured for purposes of chapter 1 of title II of the Trade Act of 1974 and section 103(d) herein, the applicable industry considered shall be limited to that of the insular possession concerned."

Fifth. Generally headnote 3(a) of the tariff schedules of the United States should be amended to increase the foreign materials limitation from 50 to 70 percent. This would compensate for the erosion of the Virgin Islands trade incentive over the course of the last decade, and provide Virgin Islands manufacturers with the flexibility needed to compete with other basin countries.

Sixth. We support additional Federal funding for the completion of the St. Thomas Airport.

Seventh. Although we support the repeal of section 1112 of the Trade Agreements Act of 1971, the same type of determination required by section 1112 should be incorporated into the proposed legislation of the Caribbean Basin Initiative. Upon request of the Governor of the Virgin Islands or the Governor of Puerto Rico, the President should be required to determine whether the various concessions granted under this legislation have resulted in injury to the economies or the industries of the Virgin Islands or Puerto Rico. If so, compensation should be provided.

Now, Mr. Chairman, we would also like to comment on some of the important tax provisions in this regard.

Mr. **Marquez.** Mr. Chairman, we have two related proposals faced by U.S. businesses interested in investing in the Virgin Islands.

The first proposal is to extend the investment tax credit and ACRS depreciation rules to property used in the possessions.

The second proposal, which has received considerably less attention, is Delegate de Lugo's long-awaited plan to place the Virgin Islands on a rough parity with other U.S. possession, by reducing the withholding tax imposed by the Virgin Islands on passive income paid to business investors.

The Virgin Islands Trade Institute fully supports both of these measures, and believes that each will play an essential role in maintaining the relative desirability of the U.S. Virgin Islands as a situs for investment by the business community.

It is well known to sophisticated tax practitioners and investors that the unique relationship between the United States and the U.S. Virgin Islands creates a perplexing array of tax rules which plagues both the business community and the Virgin Islands treasury. Historically, the "mirror system" of taxation, under which the Virgin Islands are treated as a foreign country which has adopted the U.S. Internal Revenue Code, has compelled the Virgin Islands to withhold a 30-percent tax on dividend and interest payments to the U.S. investors, including parent corporations. The 30-percent rate has greatly exceeded the withholding taxes imposed by competing jurisdictions and, to a prospective investor, has often made the Virgin Islands an unacceptable alternative to other comparable locations. Clearly, the tax must be reduced.

Over the course of the past several years, the local Virgin Islands government has engaged in an active debate regarding the desirability of sacrificing a portion of the withholding tax revenues in order to improve the investment climate. Mr. de Lugo's bill, which represents a carefully reasoned compromise between these competing interests, is intended simply to make the tax impact of investing in the Virgin Islands roughly comparable to the impact of investing in competing jurisdictions such as Puerto Rico. The Virgin Islands Trade Institute supports this measure as vital to the continued economic health of the Virgin Islands.

However, in the present economic environment, the withholding tax reduction cannot stand alone. Many U.S. companies, presently operating in the Virgin Islands and desiring to expand their operations with additional investments, are faced with the realization that, under current law, new investment in the United States is rewarded with substantial tax benefits in the form of the investment tax credit and rapid cost recovery under the new ACRS rules, while most new investment in the Virgin Islands is not eligible for either benefit. Thus, the United States tax laws have inadvertently created a compelling disincentive to invest in the Virgin Islands.

As part of the Caribbean Basin Initiative, the administration has proposed to extend the investment tax credit and the ACRS rules to property used in the possession, primarily to maintain the possessions' attractiveness to the business community vis-a-vis other Caribbean Basin jurisdictions which would benefit from the Initiative. The institute fully supports this approach, and moreover the institute emphatically urges this committee to recognize that, even in the absence of the other economic incentive provisions of the Caribbean Basin Initiative, the tax provisions for U.S. possession are essential as a means of counteracting the disincentive to invest in the possessions already created by the 1981 Tax Act.

And I may add this disincentive may be compounded if the President's new proposal on enterprise zones is adopted.

In conclusion, the Virgin Islands Trade and Economic Development Institute does not oppose a policy of assistance to our Caribbean neighbors by the United States Government. It seeks only to insure that any such policy does not destroy the hard-earned achievements of the Virgin Islands, which after all is inhabited by U.S. citizens.

Thank you, Mr. Chairman.

[The prepared statement follows:]

STATEMENT OF THE VIRGIN ISLANDS TRADE AND ECONOMIC DEVELOPMENT INSTITUTE

MR. CHAIRMAN AND MEMBERS OF THE HOUSE WAYS AND MEANS SUBCOMMITTEE ON TRADE, the Virgin Islands Trade and Economic Development Institute ("VITEDI") is pleased to have this opportunity to testify regarding H.R. 5300, the Administration's proposed Caribbean Basin Economic Recovery Act ("Act"). The Institute is an independent, non-profit organization dedicated to the promotion of economic development and business investment in the United States Virgin Islands. The Institute's members include both U.S. companies operating in the Virgin Islands, as well as local territorial businesses.

The Virgin Islands Trade Institute supports the stated goals and objectives of the President's Caribbean Basin Initiative ("CBI") and believes that a concerted effort to reduce poverty and misery in that region is long overdue. However, we believe that progress in the Caribbean Basin must not be allowed to come at the economic expense of the Virgin Islands. Recognizing that the Virgin Islands is part of both the United States and the Caribbean, we believe that such a result ultimately would thwart the purposes of the CBI.

To this end, we applaud the President's recognition of the important United States interest in the continued economic well-being of American flag territories in the Caribbean. We further note the principle established by the President in proposing the Caribbean Basin Initiative that, given the United States' "special, valued relationship with Puerto Rico and the Virgin

Islands," the economic development of these territories must be "enhanced by [United States] policy toward the rest of the region." The Virgin Islands Trade Institute, however, is concerned that H.R. 5300, while including several provisions beneficial to the Virgin Islands, does not meet the President's stated objective. Indeed, if the proposed legislation is not modified in some important respects, the Institute believes that H.R. 5300 could have a potentially devastating impact on both the economic viability of the Virgin Islands, as well as its desirability as a place to do business.

FREE TRADE ARRANGEMENT

The centerpiece of the President's proposal is the unilateral elimination of tariffs on all products other than textiles and sugar coming from designated Caribbean Basin countries -- *i.e.*, the establishment of a "one-way free trade zone" between such countries and the United States. While the overall effect on the United States mainland economy may not be significant, the impact of such a policy on the competitive position of the Virgin Islands could be disastrous. The problem is several fold.

First, because Caribbean countries are not subject to United States laws, including minimum wages, labor standards, environmental restrictions, occupational, health and safety requirements, American flag shipping limitations, as well as other regulatory burdens too numerous to mention here, foreign producers can undercut the price of goods manufactured in the Virgin

Islands. Without a tariff, there is nothing to protect industries already located or contemplating location in the Virgin Islands. Moreover, many of the Basin countries already enjoy duty-free access to the European Economic Community and other preferential treatment under the Lome Convention and various international agreements, while such treatment is denied to Virgin Islands businesses because of our relationship to the United States. By providing one-way free trade with the United States, the CBI provides a substantial advantage to Basin countries over the Virgin Islands in terms of access to world markets.

Second, it must be remembered that the Virgin Islands, too, lies outside of the customs territory of the United States and, unlike Puerto Rico, is essentially considered a foreign country for trade purposes. Thus, Virgin Islands products, unless otherwise exempted, are subject to duty when entering the United States. Historically, products of the Virgin Islands have had duty-free access to mainland markets under General Headnote 3(a) of the Tariff Schedules of the United States, which allows such products to enter the United States duty-free provided that the landed cost of such products contain no more than 50% foreign materials (or 70% foreign materials in the case of watches). However, the advantages provided by General Headnote 3(a) have eroded over the last 10 years, as inflation and the continuing rise in the price of foreign materials have prevented many of the companies that once operated profitably in the Virgin Islands from meeting the 50% test and forced them out of business.

While the Administration has proposed extending to the Virgin Islands, as an alternative to General Headnote 3(a), the same rules of origin test which it has proposed extending to the other Caribbean Basin countries, such a provision will unfortunately have little benefit for the Virgin Islands. Unlike Jamaica, the Domenican Republic or the Central American countries of the Caribbean countries, the Virgin Islands has no natural resources or indigenous materials to use in manufacturing. Consequently, unlike its Caribbean neighbors which can utilize local materials in meeting the proposed rules of origin test. Virgin Islands products could qualify for duty-free entry under the CBI formula only by adding 25% of the appraised value of such products in direct manufacturing or processing of high cost foreign materials. Of all of the industries operating in the Virgin Islands, we believe that only the Virgin Islands textile industry, which is currently depressed because of its inability to meet the 50% foreign materials test under General Headnote 3(a), could benefit by this provision. We hasten to note, however, that textiles are not eligible under the proposed free trade arrangement.

Third, in order to compete effectively with other Basin countries in light of the disparity in regulatory and other burdens, the Virgin Islands requires substantial improvements in its infrastructure. As a fundamental matter, business and industry need a dependable supply of adequate water and power. The provision of these basic services in the Virgin Islands, however, is inadequate. While the Government of the Virgin Islands has committed itself to an ambitious program to upgrade these services, the Government lacks the financial resources to complete the program.

Similarly, the Virgin Islands desperately needs new airport facilities on St. Thomas. The present runway at the Harry S. Truman Airport is only 4600 feet long and heads the list as the "most unsafe" airport in the United States. Only two countries in the entire Caribbean have airports smaller than St. Thomas. As a result of two major jet crashes in recent years involving several deaths, all but one airline have shunned landing their jet aircraft on St. Thomas. Recognizing that the lack of adequate airport facilities puts the Territory's important tourist industry at a serious disadvantage with respect to its Caribbean competitors, the Virgin Islands Government has embarked on a major expansion of its St. Thomas facilities. However, unless the Federal Government provides additional funding, the fiscally-pressed local Government will have to abandon construction short of completion.

Finally, the Virgin Islands Trade Institute wishes to note the particular impact of the proposed free trade arrangement on one of the most important local industries. The proposed elimination of the U.S. tariff on rum imported from CBI beneficiary nations poses a direct threat to both the Virgin Islands rum industry, as well as the fiscal viability of the Territorial Government. The rum industry is presently the Virgin Islands Government's largest single source of revenue, generating in 1980 over

$35 million in federal excise taxes collected on rum sold on the mainland and rebated to the Territory's Treasury. Because these funds are used to meet the general obligations of the Territorial Government, including the provision of basic services, it is essential to the rest of the business community that the Virgin Islands rum industry remain healthy and competitive.

It is, therefore, important to understand the precise nature of the risk that CBI poses to the Territory's rum industry. Virgin Islands rum, unlike that produced in Puerto Rico, is largely unaged bulk rum without brand name recognition. As such, it is significantly price elastic and thus more vulnerable to tariff reduction than Puerto Rican rum. Foreign producers, who are not subject to the same heavy environmental, wage, safety and other regulatory burdens, can manufacture the same product at lower cost. The present tariff on rum, then, constitutes the only protection which assures the continued viability of the Virgin Island rum industry. Removal of this protection, without offsetting governmental actions such as those relating to environmental requirements, would probably assure the ultimate demise of this industry.

RECOMMENDATIONS ON COMMERCIAL PROVISIONS

The people of the Virgin Islands are skilled, hard-working and industrious. They are not afraid to compete. But in order to compete and survive, the Administration's proposed legislation must be amended to insure that the Virgin Islands has the means to compete. Specifically, the Virgin Islands Trade Institute proposes the following with respect to the free trade arrangement:

1. Rum should be excluded from the list of articles eligible for duty-free treatment. Because of the excise tax rebates, rum plays proportionately even a greater role in the economies of the Virgin Islands and Puerto Rico than do the textile and sugar industries in the United States.

The Administration has acknowledged the threat to the fiscal integrity of the territories by proposing to cover over to the treasuries of the Virgin Islands and Puerto Rico the excise taxes collected on all foreign imported rum on the basis of a formula to be developed by the Secretary of the United States Treasury. For the reasons noted above, however, we expect that U.S. sales of price-sensitive, unaged bulk rum will be disproportionately affected by tariff elimination. Therefore, a formula dividing excise taxes on foreign rums between the Virgin Islands and Puerto Rico based on any factor other than loss of pre-CBI market share would probably be insufficient to make the Virgin Islands whole. Moreover, even full compensation in terms of revenues would not make up for the loss of an entire industry employing 3% of the Territory's manufacturing work force.

2. If, on the other hand, Congress decides to eliminate the tariff on rum, the Virgin Islands Trade Institute believes, as with the case of the large foreign sugar producing countries, qualifying Basin countries should be limited to a duty-free quota of up to 110% of the historical high levels of rum entering the

United States. At the same time, we believe the Virgin Islands rum industry should be exempted from undue and unnecessary regulatory burdens imposed by the Federal Government. Finally, we would recommend that the "snap-back" provision embodied in Section 104(b) of H.R. 5300 be amended so that the President will be required to consider compensatory measures, including reimposition of the duty, if the amount of excise taxes covered into _either_ the Treasury of the Virgin Islands _or_ Puerto Rico pursuant to Section 302 is reduced below the amount which would have been covered over if the imported rum had been produced in such Territory.

3. Products manufactured in the Virgin Islands, including rum, should be granted access to markets in Canada and the European Economic Community under conditions no less favorable than products manufactured in CBI beneficiary countries.

4. The "safeguard" mechanism embodied in Sections 103(d) and 104(e) provides inadequate relief. Given the fragility of the Virgin Islands competitive position, the escape clause provisions of Title II of the 1974 Trade Act would fundamentally operate _ex post facto_. Once the injury is complete and the Virgin Islands industries irreversibly lost, no amount of relief recommended by the International Trade Commission or adopted by the President of the United States would be adequate.

Additionally, Section 104(e) should be qualified to state that the expanded definition of the term "industry" does not apply to all actions arising under Chapter 1 of Title II of the Trade Act of 1974. The new definition should apply only insofar as coverage of the Trade Act is incorporated into provisions of the Caribbean Basin Initiative through Section 103(d). We do not believe that the legislative intent is to permit Virgin Island producers to bring cases before the ITC except as provided by this legislation.

Finally, the Virgin Islands Trade Institute is concerned that the purposes of Section 104(e) may be frustrated because of practical limitations imposed by the substantial injury test of the Trade Act of 1974. The duty-free tariff suspension provisions of Section 103(d) are meant to provide relief to producers in the Virgin Islands who are harmed by increased imports into the United States resulting from the Caribbean Basin Economic Recovery Act. The injury test imposed by the 1974 Trade Act, however, remains applicable to the entire U.S. domestic industry producing a like or directly competitive article.

Because of the obvious size disparities, increased Caribbean Basin imports into the United States could substantially injure or even destroy a competing industry in the Virgin Islands which is dependent upon exports to the United States, while such increased imports would hardly affect the larger U.S. industry. Unless relief is available when the Virgin Islands industry is substantially injured, regardless of the effect on the larger U.S. industry, the provisions of Section 104(e) would be meaningless. The Virgin Islands Trade Institute, therefore, recommends that Section 104(e) be amended to provide that "in determining whether an industry of a United States insular possession has been injured for purposes of Chapter 1 of Title II of the Trade Act of 1974 and Section 103(d) herein, the applicable industry considered shall be limited to that of the insular possession concerned."

5. Generally Headnote 3(a) of the Tariff Schedules of the United States should be amended to increase the foreign materials limitation from 50% to 70%. This would compensate for the erosion of the Virgin Islands trade incentive over the course of the last decade and provide Virgin Islands manufacturers with the flexibility needed to compete with other Basin countries. The Institute also supports H.R. 5738, legislation introduced by Virgin Islands Delegate deLugo, which addresses the particular problems of the Territory's watch industry.

6. The Virgin Islands Trade Institute supports additional federal funding for the completion of the St. Thomas Airport, as well as additional federal assistance for the Territory's water and power program.

7. The Virgin Islands Trade Institute supports the repeal of Section 1112 of the Trade Agreements Act of 1979 under Section 104(c). In view of Section 302 of the Act which mandates the rebate of rum excise taxes to the Virgin Islands and Puerto Rico, Section 1112 of the Trade Act of 1979 is no longer necessary.

We recommend, however, that the same type of determination required by Section 1112 of the 1979 Trade Agreements Act be incorporated into the proposed legislation on the Caribbean Basin Initiative. Upon request of the Governor of the Virgin Islands or the Governor of Puerto Rico, the President should be required to determine whether the various concessions granted under this legislation have resulted in injury to the economies or the industries of the Virgin Islands or Puerto Rico. The factors which shall be considered in such determination should include, but not be limited to, total compensation paid to such territories under Section 302, the effects on employment and wages, and an evaluation of the overall economic impact of the various provisions of Section 104.

COMMENTS ON TAX PROVISIONS

The Administration's proposed Caribbean Basin Initiative also includes important tax incentives which are designed to attract new U.S. investment to the countries of the Caribbean Basin. The Virgin Islands Trade Institute is concerned that these incentives, unless included with additional provisions to lessen the substantial tax hurdles faced by U.S. companies doing business in the Virgin Islands, will divert investment from the Virgin Islands to other Basin countries.

Currently pending before this Committee are two related legislative proposals which represent an attempt to lessen these tax hurdles. The first proposal, which is part of the Caribbean Basin Initiative, is the Administration's plan to extend the investment tax credit and ACRS depreciation rules to property used in the possessions by United States citizens and corporations.

The second proposal, which has received considerably less attention, is Delegate deLugo's long-awaited plan to place the Virgin Islands on a rough parity with other U.S. possessions, by reducing the withholding tax imposed by the Virgin Islands on passive income paid to business investors.

The Virgin Islands Trade Institute fully supports both of these measures, and believes that each will play an essential role in maintaining the relative desirability of the U.S. Virgin Islands as a situs for investment by the business community.

It is well known to sophisticated tax practioners and investors that the unique relationship between the United States and the U.S. Virgin Islands creates a perplexing array of tax rules which plagues both the business community and the Virgin Islands Treasury. Historically, the "mirror system" of taxation, under which the Virgin Islands are treated as a foreign country which has adopted the U.S. Internal Revenue Code, has compelled the Virgin Islands to withhold a 30% tax on dividend and interest payments to United States investors, including parent corporations. This 30% rate has greatly exceeded the withholding taxes imposed by competing jurisdictions and, to a prospective investor, has often made the Virgin Islands an unacceptable alternative to other comparable locations. Clearly, the tax must be reduced.

Over the course of the past several years, the local Virgin Islands government has engaged in an active debate regarding the desirability of sacrificing a portion of the withholding tax revenues in order to improve the investment climate. Mr. deLugo's bill, which represents a carefully reasoned compromise between these competing interests, is intended simply to make the tax impact of investing in the Virgin Islands roughly comparable to the impact of investing in competing jurisdictions such as Puerto Rico. The Virgin Islands Trade Institute supports this measure as vital to the continued economic health of the Virgin Islands.

However, in the present economic environment, the withholding tax reduction cannot stand alone. It is crucial for this Committee to understand the devastating effect that the Economic Recovery Tax Act of 1981 may have on the Virgin Islands unless the Administration's tax measures for the possessions, as well as the withholding tax reduction, are enacted into law. Many U.S. companies, presenting operating in the Virgin Islands and desiring to expand their operations with additional investments, are faced with the realization that, under current law, new investment in the United States is rewarded with substantial tax benefits in the form of the investment tax credit and rapid cost recovery under the new ACRS rules, while most new investment in the Virgin Islands is not eligible for either benefit. Thus, at a time when the business community and the Virgin Islands government have reached agreement on a mutually beneficial means of expanding the Virgin Islands economy, the United States tax laws have inadvertently created a compelling disincentive to invest in the Virgin Islands.

As part of the Caribbean Basin Initiative, the Administration has proposed to extend the investment tax credit and ACRS rules to property used in the possessions, primarily to maintain the possessions' attractiveness to the business community vis-a-vis other Caribbean Basin jurisdictions which would benefit from the Initiative. The Institute fully supports this approach, and agrees with the Administration that the United States has a special responsibility toward its possessions. Moreover, the Institute emphatically urges this Committee to recognize that, even in the absence of the other economic incentive provisions of the Caribbean Basin Initiative, the tax provisions for U.S. possessions are essential as a means of counteracting the disincentive to invest in the possessions created by the 1981 Tax Act.

Finally, the Institute wishes to call to the attention of this Committee the serious revenue shortfalls which the Virgin Islands Treasury is facing as a result of the 1981 tax cuts. When these tax cuts were enacted in the United States, it was anticipated that the immediate reduction in revenues would ultimately be offset by an enlarged tax base, as increased after-tax personal and business income translated into increased savings and investment. However, the Virgin Islands, which, by virtue of the "mirror system," suffers a parallel reduction in current revenues, anticipates no resultant increase in its tax base, for the simple reason that the pool of Virgin Islands investment dollars is not internally generated, but comes predominantly from the United States. Thus, the Virgin Islands expects to reap no significant benefits from the 1981 tax cuts, unless the cuts have the intended effect of increasing investment and a significant amount of that investment is directed toward the Virgin Islands.

Because of this unique revenue impact of the 1981 tax cuts on the fiscal integrity of the Virgin Islands Treasury, the Virgin Islands may no longer be in a position to offer substantial investment incentives in the form of tax subsidies and reductions. Mr. deLugo's bill recognizes the threatened harm to the Virgin Islands Treasury, and mitigates this effect to some extent by modifying the foreign tax credit provisions applicable to the Virgin Islands. It is expected that the relaxed credit will render it unnecessary for the Virgin Islands to reduce the withholding tax below the compromise rate of 10%.

The Institute fully supports this measure, in the hope that the Virgin Islands, painfully squeezed by low tax rates in competing jurisdiction and drains on its own Treasury caused by the 1981 tax cuts, will find it possible to offer the business community a reasonably favorable tax environment.

In conclusion, the Virgin Islands Trade and Economic Development Institute does not oppose a policy of assistance to our Caribbean neighbors by the United States Government. It seeks only to insure that any such policy does not destroy the hard-earned achievements of the Virgin Islands, which, after all, is inhabited by United States citizens.

Chairman GIBBONS. Thank you.

Do you have a statement?

Mr. KIMMELFIELD. No.

Chairman GIBBONS. Let's go back to the Schenley plant down there. Have any of you all heard complaints from any of the local residents about effluent coming out of the plant?

Mr. HIEBERT. I think that is a question that more properly ought to be asked of the Schenley representative.

Chairman GIBBONS. Well, you are residents of the Islands, and I am just calling on you to see if there is any local problem with that effluent. I said yesterday I would work with Mr. de Lugo in trying to get that provision removed. I am for clean water, but if we are going to dump it where it's 27,000 feet deep——

Mr. MARQUEZ. Sir, I believe part of the problem is not so much the Virgin Islands, but with Puerto Rico. I understand that the effluent in Puerto Rico is discharged into the bay. That is not the case with the distilleries in the Virgin Islands, because they are located on the south coast of St. Croix. I believe they have an 1,800 foot outfall, which pretty much disperses the effluent in deep water, and that effluent does not interfere with the land.

I believe that is the reason why, but the EPA has——.

Chairman GIBBONS. Well, I will certainly talk to the EPA about it and see what can be done, and with your representative in Congress.

Mr. MARQUEZ. I understand that the cost of the treatment exceeds the cost and value of the distilleries.

Chairman GIBBONS. Yes, that was in the statement by the gentleman from Schenley.

Mr. HIEBERT. We appreciate your interest, Mr. Chairman.

Chairman GIBBONS. Too bad you cannot find something to do with that effluent.

I support the idea you have of removing the withholding tax on passive income. I think that is a productive step to be taken, and I see no reason why we cannot include Mr. de Lugo's bill in this bill, so it would all move forward together. I do not want to hold his bill up, in case it could get through any sooner, but I do not know why we cannot just go ahead and get that done at this time.

Your watch industry. Yesterday we were talking about apparently reducing the domestic content of the watches. I don't know exactly what you are advocating.

Mr. HIEBERT. I am not that familiar with the watch bill, myself, but my understanding is that it might have been explained a little better yesterday than it was. My understanding is that the bill would allow duty-free entry of watches based on a system of rewards; that is the more labor you put into the watch, the better off you are going to be. But there is no intent to do any less manufacturing in the watch industry as a result of this bill. If anything, it is designed to encourage more manufacturing operations down there, but because of the problem posed by, I believe, digital and electronic watches, the watch industry does require additional flexibility beyond the 70 percent test that is currently available to them under 3(a).

Mr. MARQUEZ. There was a concern that there would be a passthrough. My understanding of the bill is that it requires local input, local work processes and as a result of that, local manufacturers would get certificates which would then be available to offset the duty. That is the incentive for doing the work in the Virgin Islands. So it is not just a straight pass-through bill. It would encourage local input.

I am not very familiar with the bill, like Peter says, but that is my understanding of it.

Chairman GIBBONS. Is there a differential between the minimum wage in the Virgin Islands and the mainland, or is it the same?

Mr. MARQUEZ. The minimum wage is the same in the Virgin Islands as on the mainland. The average industrial wage, I believe, is different.

Chairman GIBBONS. How long has the Virgin Islands been at the minimum wage requirement, do you know?

Mr. HIEBERT. I believe it goes back to the late 1950's, but at that time I believe there was also a disparity between the minimum for workers on the mainland and workers in the Virgin Islands and Puerto Rico. Over the course of the last 25 years, that discrepancy has been gradually eliminated. Right now our minimum wage is the same as on the mainland.

In point of fact, I believe the average manufacturing wage in the Virgin Islands is almost comparable, if not perhaps even a little bit higher, than the average manufacturing wage in some of the southern States, and this puts us at an extreme disadvantage, from a competitive point of view, with respect to other Caribbean competitors.

Chairman GIBBONS. I realize that increasing the length of the runway on St. Croix would be important economically, and I know that increasing the length of the runways on St. Thomas is important, from a safety point of view. I think it would be helpful if we could get some firm assurances from the administration that they at least plan to finish the St. Thomas runway at the earliest possible date, because I know how dangerous that situation is.

Mr. HIEBERT. Absolutely, Mr. Chairman. I couldn't agree with you more. I'd just like to point out what this new airport can mean to the Virgin Islands. At the present time we cannot bring in large jet aircraft to St. Thomas. That means we can't bring in charter jets as well, which means that we cannot take maximum advantage of the business groups convention deduction and attract business to the islands.

Mr. MARQUEZ. Also, the irony is that phase I has been pretty much completed, and we have performed an engineering miracle in bringing down two mountains and extending the runway into the sea, into 90 feet of water. Yet you cannot land planes because while you have the landfill, you don't have the runways available which are to be built as part of phase II, or the terminal, and the future taxiways which are to be built as part of phase III. So even though you have a landfill on the islands, you can't use it.

Chairman GIBBONS. How long has the landfill been complete?

Mr. HIEBERT. I believe it will be complete in June.

Chairman GIBBONS. And you do not have a commitment from the government?

Mr. MARQUEZ. No, sir.

Mr. Hiebert. The other thing that should be noted is that if construction has to be halted because additional Federal funds are not forthcoming, that would add $5 to $7 million to the cost of the project just in demobilizing the effort that is already in place.

Mr. Marquez. We also have an 18-percent inflation rate per year, so it's going to cost next year 18 percent more to do the work.

Chairman **Gibbons.** Mr. Bailey?

Mr. Bailey. Thank you, Mr. Chairman.

You mentioned the investment tax credit, and the ACRS. Has anyone given you, or have you studied, or have you read anywhere what the impact will be on the Virgin Islands?

And, second, I do not understand—do you plan to replace this 30 percent withholding capacity?

Mr. Kimmelfield. I'd like to ask for clarification. Are you asking what the impact of the rules would be on the Virgin Islands revenue?

Mr. Bailey. On investment in the Virgin Islands. Have you done any work on that effect? Some investment would leave as a result of the application of the investment tax credit, to accelerate depreciation of recovery systems in the Caribbean Basin countries, in light of the competition for the wage rate and OSHA requirements and that sort of thing.

Mr. Marquez. I don't think that we would see a loss of industry already there, but I think it is going to make it that much more difficult to bring new industry in.

Mr. Kimmelfield. I was going to say that same thing.

Mr. Bailey. That arithmetic comes down on the side of what?

Mr. Kimmelfield. Are you speaking of extending the administration proposal?

Mr. Bailey. Maybe you are not aware that the administration proposal would extend the benefits for American investments in the CBI countries, along with the advantages of accelerated depreciation that presently can be enjoyed. I assume that would include investment tax credit advantages, and would hopefully include, once you are able to discourage the administration from pursuing this very counterproductive alternative corporate tax idea, all of those advantages are going to be extended, you see, to the other CBI countries.

Now I don't know if it's more than a plum. It looks good, but I just wonder whether it really means anything to you. I cannot see where it really would make you that much more attractive for investment purposes. It certainly gives you no special advantage.

Mr. Kimmelfield. There are two problems, in the absence of the extension of these rules to investment in the Virgin Islands:

One is that in the absence of such an extension, there is a disincentive to invest in the Virgin Islands as opposed to additional investments in the United States.

Mr. Bailey. That was the second part of my question. Does that 30 percent problem——

Mr. Kimmelfield. No, there are two different—there are two interrelated solutions to the problem; the reduction of the 30- to 10-percent withholding rate is a long-range solution for a company considering how their earnings are going to be repatriated. But the problem of the accelerated depreciation and the investment tax credit is that in the immediate picture, a company investing in the United States is going to improve its tax picture in the current year; whereas a comparable investment in the Virgin Islands will have no effect.

Mr. **Bailey**. But my question was, Does the CBI change that?

Mr. **Kimmelfield**. The CBI will certainly make the Virgin Islands investment comparable in the tax year in which the investment is made to U.S. investment.

Mr. **Bailey**. I realize that. Is the 30 percent, so-called—is that being changed by the Caribbean Basin Initiative?

Mr. **Kimmelfield**. That change is in a separate bill which has been introduced as H.R. 5113.

Mr. **Bailey**. Is that the bill the chairman referred to?

Mr. **Kimmelfield**. I believe so.

Mr. **Bailey**. But it's a part of the administration's proposal?

Mr. **Kimmelfield**. That is correct.

Mr. **Bailey**. And so we don't have any understanding to go back and talk about the advantages of the tax credit and the accelerated depreciation and putting it on an equal footing with the mainland. The consensus usually appears to be that the net impact of those advantages does not really benefit the Virgin Islands, in light of the fact that those will be extended to American subsidiaries in other Caribbean Basin Initiative countries.

Mr. **Kimmelfield**. That's correct.

Mr. **Bailey**. Is that correct?

Mr. **Kimmelfield**. That's correct.

Mr. **Bailey**. OK.

That's all the questions I have. Thank you very much.

Chairman **Gibbons**. Thank you very much.

Next we have Mr. Mitchell Cooper, of the Rubber Manufacturers Association.

STATEMENT OF MITCHELL COOPER, COUNSEL, FOOTWEAR DIVISION, RUBBER MANUFACTURERS ASSOCIATION

Mr. **Cooper**. My name is Mitchell Cooper. I am testifying as counsel for the Footwear Division, Rubber Manufacturers Association. The companies in this division, whose names appear on attachment 1 to my testimony, account for most of the waterproof footwear and rubber-soled footwear with fabric uppers produced in this country.

I should note at the outset that one of these companies, Nike, Inc., imports a large share of the rubber footwear that it sells in this country, and has asked to not be associated with this testimony.

The duties on these types of footwear vary from 20 percent to 67 percent. With one very minor exception, these duties were not cut in either the Kennedy round or the Tokyo round of the multilateral trade negotiations.

Moreover, both waterproof and fabric upper rubber-soled footwear are excepted by statute from GSP duty reductions.

Rubber footwear is a labor-intensive, import-sensitive industry. It has had the attention and concern of many Government agencies for many years. In September 1981, the Department of Defense examined into the capability of the waterproof segment of this industry to meet defense requirements and concluded that, and I quote,

> * * * loss of one or two of our current major suppliers would seriously jeopardize our ability to meet military requirements under surge/mobilization conditions.

In June 1981, the Department of Commerce issued a report on domestic and import competition in the rubber footwear industry. I believe that the staff of this committee has copies of both the Defense and Commerce reports, and I shall not burden the record with additional copies of them.

I do, however, think it particularly relevant to the subject matter of these hearings that you have an awareness of what has happened to domestic shipments and imports of these high-duty items, and I am therefore appending as attachment 2 a copy of the table which appears on page 13 of the Commerce Department's report.

You will note the steady decline in domestic shipments and the steady increase in imports of rubber-soled footwear with fabric uppers between 1964 and 1980. In 1980, imports took 60.6 percent of our domestic market. There is reason to believe that when the 1981 figures are available, they will show an even higher ratio of imports to consumption.

In recent years, close to 90 percent of the imports of rubber footwear have come from the low-wage countries of the Far East, notably Taiwan and Korea, and more recently the People's Republic of China.

Attachment 3 to this testimony, which is also taken from the Commerce Department report, shows hourly compensation for rubber footwear workers in Korea, Taiwan, and the United States. In 1979, the last year for which comparative data are available, the figure for Korea was between 80 and 83 cents and for Taiwain was between 87 and 91 cents; whereas in the United States hourly compensation was $5.90.

According to the Commerce Department, footwear workers in the People's Republic of China are paid an estimated 20 cents an hour. China has become the third largest exporter of rubber footwear to this country, sending 9 million pairs in 1980.

Bear in mind that this large volume of imported rubber footwear comes to this country from thousands of miles away at high rates of duty. There are today rubber footwear capacity and skills in the Caribbean Basin, notably in the Dominican Republic. If the 20–67 percent duties on rubber footwear are eliminated for this area of the world, what is left of this domestic industry will indeed be in jeopardy. Plants in States such as Georgia, Maine, Pennsylvania, Massachusetts, Illinois, and Florida will have a great incentive to shift their production to this low-wage, duty-free area, and importers from the Far East will readily shift gears to take advantage of this new duty-free source of supply. The competitive advantage that importers already have over their domestic counterparts will prove devastating.

Nor is the concern of this industry alleviated by the provision in the bill before you which calls for expeditious action by the International Trade Commission on a petition alleging import injury or the threat of import injury. There is no relevant information on the question of import injury to the rubber footwear industry which the Government does not already have. It would be an unconscionable burden on such a small industry to require it to go to the expense of making a self-evident case based on data with which Government agencies are now thoroughly familiar. And given the right of the President to overrule an ITC finding on grounds other than economic injury, I think you can understand the lack of confidence the rubber footwear industry has in the so-called escape clause procedure.

The President has seen fit to exempt textiles and apparel from the free-trade provision of this bill. I submit to you that the claims of the rubber footwear industry for an exemption are at least as valid as those of the textile and apparel industry.

We fully appreciate the urgency of some kind of Marshall plan approach to the critical economic problems of our neighbors to the south, but the burden of assistance should not be borne by the companies and workers of an industry such as rubber footwear where high duty, low-wage imports have already taken some two-thirds of our domestic market.

And if I may just add a word, Mr. Chairman, in light of the very interesting testimony which has already been placed into the record this morning, for a number of years I have served as Washington counsel for the Manufacturers Association of Puerto Rico, and in that capacity I was witness to the ability of low-wage industries in the Far East, and indeed of industries in Haiti and the Dominican Republic, which competed with labor-intensive industries not only in the mainland United States, but in Puerto Rico as well, to have a remarkable competitive advantage over those industries, largely because of their ability to compete on a wage basis, despite this tariff structure which favored Puerto Rico.

I might point out that the footwear industry has several companies which used to be in Puerto Rico and are no longer there, having lost out to competition from the Far East.

There is still one very substantial footwear company in Puerto Rico, Converse Rubber Co., whose sole advantage over the Caribbean, one very valid reason for that company to have a plant in Puerto Rico—better than, let's say, for example, the Dominican Republic—is because it does currently have the advantage of no duty to the mainland of the United States.

Eliminate that advantage, and while I cannot speak for Converse on this question, it would seem to me that the probability, or at least the strong possibility, exists that a company such as that would find it feasible to shift some of its operations elsewhere. Multiply that problem when you have companies on the mainland of the United States whose average hourly earnings are considerably larger than in Puerto Rico, and I think you can appreciate the kind of threat that the domestic industry fears from this proposal, which I must say with all due respect to Ambassador Brock, whom I do have a great deal of respect for, and his colleagues, I do not think was fully thought through, when it was determined to remove, in effect, 13 percent of the trade from the GSP statute, which has been held to be import-sensitive, and therefore has been exempted from GSP treatment, to remove that exemption with respect to the Caribbean.

Thank you, sir.

[Attachments to the prepared statement follow:]

Attachment No. 1

MEMBERS OF FOOTWEAR DIVISION OF THE RUBBER MANUFACTURERS ASSOCIATION

Bata Shoe Company	Belcamp, Maryland
Converse Rubber Company	Wilmington, Massachusetts
Etonic, Inc.	Brockton, Massachusetts
Gold Seal Rubber Company	Boston, Massachusetts
Hyde-Spotbilt Athletic Footwear - Saucony	Cambridge, Massachusetts
Kaysam Corporation of America	Paterson, New Jersey
LaCrosse Rubber Mills Company	LaCrosse, Wisconsin
New Balance Athletic Shoes USA	Boston, Massachusetts
NIKE, Inc.	Beaverton, Oregon
Prevue Products Company	Manchester, New Hampshire
Tingley Rubber Corporation	S. Plainfield, New Jersey

Attachment #2

Rubber-Soled Canvas-Upper Footwear: U.S. Shipments, Imports, Exports, Apparent Consumption

Quantity (1,000 pairs)

Year	Shipments 1/	Imports	Exports	Apparent Consumption	Ratio Imports to Consumption
1964	162,151	29,063	255	190,989	15.2
1965	165,741	33,363	195	198,909	16.8
1966	157,491	35,060	167	192,384	18.2
1967	153,656	44,659	211	198,104	22.5
1968	158,451	49,200	239	207,412	23.7
1969	142,295	44,463	195	186,563	23.8
1970	144,276	49,726	129	193,873	25.6
1971	156,489	62,872	112	219,249	28.7
1972	159,239	58,020	105	217,154	26.7
1973	153,551	66,291	29	219,913	30.2
1974	144,496	67,352	1010	210,838	31.9
1975	132,876	73,083	564	205,395	35.6
1976	119,771	115,355	733	234,393	49.2
1977	88,691	106,012	780	193,923	54.7
1978	81,627	172,706 2/	644	253,689	68.1
1979	83,214	111,392	1218	193,388	57.6
1980	80,283	120,801	1694	199,390	60.6
Averages:					
1971-75	149,330	65,524	364	214,490	30.5
1976-80	90,717	125,253	1014	214,956	58.3

Source: Official Statistics of U.S. Department of Commerce

1/ Production data, 1970-80:

1970 - 137,194
1971 - 157,603
1972 - 153,621
1973 - 150,654
1974 - 146,500
1975 - 131,155
1976 - 115,354
1977 - 88,213
1978 - 79,278
1979 - 78,130
1980 - 72,537

2/ Includes large quantity of footwear designed to meet "rubber" footwear specifications in order to overcome limitations of Orderly Marketing Agreements with Taiwan and Korea on nonrubber footwear.

Attachment #3

Average Hourly Wages and Estimated Hourly Compensation for Workers Producing Rubber and Plastic Footwear in Korea, Taiwan and the United States

(in U.S. dollars)

Published Average Hourly Earnings

Year	Korea	Taiwan	United States
1972	.16	NA	2.82
1973	.16	.38	2.99
1974	.22	.35	3.17
1975	.25	.40	3.35
1976	.32	.52	3.49
1977	.43	.63	3.64
1978	.55	.71	3.80
1979	.69	.75	4.12

Estimated Total Hourly Compensation

Year	Korea	Taiwan	United States
1972	.18-.19	NA	NA
1973	.18-.19	.44-.46	NA
1974	.26-.27	.41-.48	NA
1975	.29-.31	.46-.48	4.55
1976	.36-.38	.60-.62	4.82
1977	.49-.51	.72-.75	5.11
1978	.63-.66	.82-.85	5.42
1979	.80-.83	.87-.91	5.90

Source: Data on Korea and Taiwan extracted from a table prepared by the U.S. Department of Labor, Bureau of Labor Statistics, Office of Productivity and Technology, March 1980; data on United States from U.S. Department of Labor, Bureau of Labor Statistics, Employment and Earnings.

SUMMARY OF TESTIMONY OF THE FOOTWEAR DIVISION, RUBBER MANUFACTURERS ASSOCIATION

The duties on waterproof footwear and rubber-soled footwear with fabric uppers are high, ranging from 20% to 67%.

With one minor exception these duties were not reduced in either the Kennedy Round or the Tokyo Round, and all rubber footwear is excepted from GSP duty reductions.

This is a labor-intensive, import-sensitive industry as to which several Government agencies have expressed concern.

There has been a steady decline in domestic shipments and a steady increase in imports of rubber-soled footwear with fabric uppers. Imports now take well in excess of 60% of the domestic market.

Close to 90% of the imports come from Taiwan, Korea, and the People's Republic of China, in all of which countries wages are substantially lower than in the United States. Despite the thousands of miles from the marketplace and the high rate of duty, such imports have had no trouble in competing against the domestic industry.

Both capacity and skills for the manufacture of rubber footwear exist in the Caribbean Basin, and elimination of duties would seriously threaten what is left of the domestic industry.

The escape clause provision in the bill does not alleviate the problem. The Government already has the relevant information regarding import injury and the danger of additional injury to the rubber footwear industry. This industry should not be called upon to bear the burden and the expense of making a self-evident case, particularly when the President would have the right to overrule an ITC finding.

Conclusion: There are no grounds for exempting the textile and apparel industries from the duty-free provision of the bill which do not apply with at least as much validity to the rubber footwear industry. The burden of assistance to the Caribbean Basin should not be borne by an industry where high-duty, low-wage imports have already taken about two-thirds of our domestic market.

Chairman Gibbons. Thank you, Mr. Cooper.

Mr. Bailey?

Mr. Bailey. Can you tell me, Mr. Cooper, how many people are affected in this country, how many jobs, from the spinoff of that?

Mr. Cooper. I can tell you the number of jobs. It's approximately 15,000. It used to be closer to 30,000.

Mr. Bailey. Sir, you are aware of the testimony we had here by the people in the leather goods area. We were talking about approximately 250,000, and we were talking about suppliers and that kind of thing. Generally speaking they said there was a relationship of about two production jobs to one in terms of service, supply, transportation, et cetera, associated with the transportation industry. A net loss of over 300,000, probably 330,000 jobs.

You're talking 15,000. Does that include the spinoff?

Mr. Cooper. No, I'm talking about direct production labor only.

Mr. Bailey. Where are these people located?

Mr. Cooper. Well, some in Pennsylvania.

Mr. Bailey. Where in Pennsylvania?

Mr. Cooper. The Carter Rubber Co., which is not a member of this association, I am not sure where their plant is in Pennsylvania. But the larger operations are in Massachusetts, Georgia, and Florida. The Pickens Rubber Co., in Georgia.

Mr. Bailey. What is the relationship now? Are we talking 20,000 jobs, or what?

Mr. Cooper. I cannot put a total figure on that, Mr. Bailey. I can only say that when we talk about a possible loss of 15,000 jobs, and the investment in the plants, what we are really saying is in those communities where those jobs are perhaps the most vital ones in the community, then you would devastate the town.

Mr. Bailey. I want to ask you a question. There is a shoe or a boot produced in the United States. It is used in hot climates. It has an overlapping steel plate on the shoe. It has rubber or some kind of rubber-like heel and sole. It has canvas, it has leather as part of this boot. Where is that boot made?

Mr. Cooper. I'm not sure where that boot is made, but a great many of the boots made for the Defense establishment are the Bata Shoe Company here in Belcamp, Md.

Mr. Bailey. I know it's made in the United States.

Mr. Cooper. I don't know the specific company that makes that specific boot. I will tell you that Bata—and there are other companies—that Bata, for example, does do a vital job for the defense industry which it could not do but for its production of athletic footwear, tennis shoes, to sustain that industry, to sustain the production for the Defense Department.

Mr. Bailey. Well, if we are going to be paying through the nose and people want to know why we have got defense spending problems, and somebody is sitting out on an M-1 tank and they want to know why our trade policies sometimes lapse, this is an example of some of the difficulties we had.

But you say it would be 15 or 20,000 jobs?

Mr. Cooper. A minimum, I think.

Mr. Bailey. However, we are heading toward half a million.

Mr. Cooper. Say that again, sir. I'm sorry.

Mr. **Bailey**. On total job loss, we are heading toward half a million jobs directly being affected.

Let me ask you about the pass-on or add-on. Right now do any of these products come through and have a value added in the Caribbean?

Mr. **Cooper**. Minimal.

Mr. **Bailey**. I want to ask this question: Why did the Caribbean Basin Initiative change the percentage from 35 percent domestic content to 25 percent? I think that is the right figure. Why is that? That part of it I cannot understand. I'm sure there is a reason for it, but I don't understand it.

Mr. **Cooper**. I must confess, Mr. Bailey, I have not focused on that aspect of the bill, because the threat of the duty-free trade for the completed product is itself so great that this is a major concern in this bill, and the consequences of that aspect of the bill alone can be so serious for this industry that the rest of it is——

Mr. **Bailey**. Do you have any industry located in the Virgin Islands or Puerto Rico?

How many employees down there?

Mr. **Cooper**. I don't know what the current employment is. I would guess that the current rubber footwear employment in Puerto Rico has got to be somewhere between 700 and 1,000 employees.

Mr. **Bailey**. What kind of people work in the plants? What is their background? Yesterday we had testimony that many of the people in the luggage area are disproportionately blacks and Hispanics, and they have enough unemployment problems as it is.

What is the proportion?

Mr. **Cooper**. It would vary from location to location, but the largest mainland rubber footwear company is in the district of Congressman Rose in North Carolina, and that is a remarkable plant because there there truly is integration. Over 50 percent of the employees are either black or Native American Indian, oddly enough. And, of course, they are in all levels of production and management. That is a beautiful textbook case of how integration can really work in this country.

There was what had been the largest plant in this country in Naugatuck, Conn., a Uniroyal plant, which at one time employed some 3,000 people, and which as a result of the extraordinarily high wage structure that they had, has now gone under. That plant no longer exists. But there there were people who had worked in this industry for 25, 30, or 40 years; families, husbands, wives, and sons. That plant has gone under. The Uniroyal plant in Georgia, as well, two plants in Georgia. The products of those plants were purchased by Striderite, and those products are now being imported from the Far East.

Mr. **Bailey**. What about U.S. Keds?

Mr. **Cooper**. They are not U.S. Keds any more, they are Keds.

Mr. **Bailey**. I just hope we can solve some of these problems with this thing.

I thank you.

Mr. **Cooper**. I thank you very much, sir.

Chairman **Gibbons**. Mr. Jenkins?

Mr. **Jenkins**. Thank you, Mr. Chairman.

Do you know the average wage scale?

Mr. **Cooper**. No, sir, I do not have access to that figure. I am proceeding from the same assumptions that I suppose many of you are proceeding from; namely, that those wages would be substantially lower, average wages would be substantially lower from the minimum wage in this country.

Mr. **Jenkins**. Would the average wage of the U.S. shoe industry normally be about $6 an hour?

Mr. **Cooper**. That's correct, sir.

Mr. **Jenkins**. Are you now paying roughly seven times the average labor cost of the Far East?

Mr. **Cooper**. That's correct, sir. And wages, if I may say so—labor constitutes roughly 50 percent of the total product in this industry.

Mr. **Jenkins**. And the total figure of imports in the shoe industry is now approaching 70 percent; is that correct?

Mr. **Cooper**. Sixty-five would be my guess for 1981; over 60 percent for 1980.

Mr. **Jenkins**. In Puerto Rico, they have lost substantial apparel industries, textile industries, and you now have remaining in Puerto Rico only one source. Is that correct, sir, as far as you know?

Mr. **Cooper**. Are you talking about rubber footwear or nonrubber footwear? Well, there is a plant in Puerto Rico and there may be one other plant in Puerto Rico, but far fewer than had been there 10 years ago.

Mr. **Jenkins**. Mr. Cooper, if we proceed along the direction that we are going and include footwear in the duty-free treatment, your clients really have no other alternative, they've got to establish facilities in these other countries, don't you?

Mr. **Cooper**. I think economic survival is likely to require that, Mr. Jenkins.

Mr. **Jenkins**. That has been, of course, what's hurting them in the past 10 years, as the domestic industry could not survive and they commenced to invest in overseas plants.

Mr. **Cooper**. Precisely.

Mr. **Jenkins**. I would assume occasionally there would be loans?

Mr. **Cooper**. I assume that to be the case.

Mr. **Jenkins**. It is very difficult for me to understand, it is very difficult for me to justify to my people, with some 1,500 or 2,000 employees in my district, with 16 percent unemployment in one particular area of my district, to justify the closing of these plants and placing these employees, who are not trained in high technology and no longer have the benefits of trade adjustment relief, to pitch those people out on the street after 13 weeks with no other industry in town, simply for this one particular bill. And very honestly, you don't have much left of the marketplace?

Mr. **Cooper**. No, sir. No, sir.

Mr. **Jenkins**. As I understand the shoe industry generally, those employees, while extremely good employees, are generally not trained in any other technology; is that correct?

Mr. **Cooper**. Well, I personally could not generalize. I would say that in rubber footwear, for example, most of the skills are not too difficult to come by. And in noting this, I would say that I was a little disturbed to read Ambassador Brock's testimony before this committee when he discounted the threat of the Caribbean becoming a significant factor in footwear, either nonrubber or rubber, because of the very minimal amount that is currently coming from the Caribbean. And it made me doubly conscious of the fact that when I started to represent the Rubber Footwear Industry in 1964, 70 percent of the imports came from Japan. Virtually none from Korea. It was very simple. We started an industry in Korea and Taiwan, and now the People's Republic of China. It is very simple to move equipment and to train people to make this.

Mr. **Jenkins**. Well, I know every Member is parochial as far as his own or her own district is concerned. It is impossible for me to justify the potential closing of plants in one of my small towns that really accounts for one-third of the total manufacturing jobs in that county, and very honestly I do not see how they have survived thus far.

So if we are unable to make any accommodation in this area, then I do not see how I could support the legislation.

I appreciate your testimony.

Mr. **Cooper**. I appreciate all the help you have rendered this industry, Mr. Jenkins.

Chairman **Gibbons**. Thank you, Mr. Cooper.

Mr. **Cooper**. Thank you very much.

Chairman **Gibbons**. Our next witness is from the committee for 806 and 807.

STATEMENT OF CAMERON CLARK, JR., PRESIDENT, COMMITTEE FOR 806.30 AND 807, INC., ACCOMPANIED BY RALPH A. BIEDERMAN, VICE PRESIDENT

Mr. **Clark**. Mr. Chairman, I would like to summarize our statement with the understanding that it will be placed in the hearing record in full.

As chairman of the Committee for 806.30 and 807, Inc., I want to thank the subcommittee for receiving our testimony. I am president of my own company, Production Sharing International, Ltd., which has operations in Central America and the Caribbean area.

With me today is Dr. Ralph Biederman, who is vice president of our committee and director of corporate relations for the Brunswick Corp.

Mr. Chairman, the Committee for 806.30 and 807 Incorporated strongly supports the enactment of the Caribbean Basin Economic Recovery Act. We believe the administration's Caribbean Basin Initiative is in the national interest of the United States, strategically, economically and commercially.

Strategically, the area's importance to the United States demands we take every feasible measure to encourage growth in the context of private initiative and stable, responsive government. It is essential that conditions be created that once again restore political stability to the total region.

Economically, the program can restore confidence and become an engine for widespread development in the region, with long-term benefits to the United States.

Commercially, the development of the program lies in nontraditional exports. Such exports can increase needed foreign exchange earnings so essential to the economies of these small countries.

The expanded trade opportunities resulting from the one-way free-trade area, combined with a tax investment incentive, can be an extremely powerful stimulus to both local and foreign investors to expand the production base of these Caribbean Basin economies.

Our Committee for 806.30 and 807, Inc. has members who already have plants assembling U.S.-made components in at least 13 of the more than 20 small nations in Central America and Caribbean area.

As this subcommittee is aware, these plants process and assemble U.S. materials and components and utilize the special duty provisions of tariff items 806.30 and 807.00 upon return of the articles to the United States.

In Central and South America, these assembly operations, for the most part, are designed to employ workers in labor-intensive operations. The labor performed in these operations is unavailable in the United States or is not available in quantities and at costs which permit total U.S. manufacture at prices competitive with direct imports into the United States.

In operating these plants in the Caribbean, we live with economic, social, and political conditions of the Caribbean Basin. We have become increasingly concerned at the decline in those conditions in recent years. They stand in stark contrast to the potential for economic progress that could be realized through trade development.

We are very much aware that the great increase in the cost of oil beginning 8 years ago has placed an enormous burden on most of the small economies. As participants in these economies, we are constantly reminded that earnings from traditional exports such as sugar, coffee, and bauxite have fallen.

As needed imports have increased in price due to inflation in the industrialized countries, the result for the Caribbean Basin has been crippling balance of payment deficits and dangerously declining international reserves.

Our members daily observe the impact of high levels of inflation in these countries as the workers have to deal with declines in real income. High interest rates and the general lack of credit choke new investment opportunities and discourage economic growth.

These conditions our members see and experience first hand. Thus, we support the administration's initiative to foster general economic progress and improvement in social conditions in the Caribbean Basin. But the question of political stability cannot be ignored. The strategic importance of the Caribbean-Central American area demands that the United States take every feasible measure to encourage economic growth in the context of private initiative and stable, responsive government.

The expanded access to the U.S. markets, coupled with the investment incentives through tax inducements, and further assurances of the bilateral investment treaties and investment assistance and insurance through the Overseas Private Investment Corporation, all combine to open up private enterprise opportunities in the Caribbean Basin.

With imaginative support of medium-term credit or credit guarantees, possibly to indigenous commercial banks, by the Export-Import Bank, the Caribbean Basin Initiative can contribute to a dramatic turnaround in the area's economic decline.

In short, this integrated program of self-help, emphasizing the role of private enterprise, provides an umbrella for more effective evolution of relations between the private sectors in the beneficiary countries and in the United States. It can restore confidence and become the engine for widespred economic development in the region.

In this overall effort, we have the cooperation of Canada, Mexico, and Venezuela, each country having pledged to continue their own unique economic assistance programs in this area. Our European and Japanese trading partners have expressed support and promised assistance, where appropriate.

In overseas operations under tariff items 806.30 and 807.00, we have also seen the benefits that production sharing enterprises can bring to these small countries, in terms of increasing employment and incomes, upgrading labor skills, and creating a demand for auxiliary and support services.

The free trade area proposed in the Caribbean Basin Initiative would permit all imports from beneficiary countries to enter the United States free of duty, except for textiles and apparel articles subject to the multifiber agreement and the supporting bilateral agreements on textiles and apparel. The free trade area would be in effect for a period of 12 years—a necessary time requirement to initiate investment plans and realize investment returns.

U.S. imports from the 20 countries and semi-independent island nations were $10 billion in 1981, and of that total, $6 billion were U.S. imports from the Bahamas, Trinidard, and Tobago, and the Netherland Antilles, mostly exports of crude petroleum and refined petroleum products. In total 87 percent of the imports from the Caribbean Basin countries currently are virtually duty-free. It is the potential represented by the 13 percent which makes the free trade area so vital to the countries of the Caribbean Basin.

The potential lies in the nontraditional exports of the traditionally underdeveloped economies, not raw material and tropical products, but manufactured and processed articles—many of which are adaptable to production-sharing arrangements.

These nontraditional exports can increase needed foreign exchange earnings so essential to the economies of these small countries. Such export-led development can benefit U.S. industries and workers by expanding markets for U.S. exports. Where they are feasible, production-sharing arrangements can increase competitive ability of U.S. goods in the domestic market and abroad.

Attached to this statement is table 1, showing total 1981 imports and free and dutiable imports from each country in the Caribbean Basin.

There are two elements of the proposal for the free trade area that must be considered. The Committee for 806.30 and 807, Inc. is very sensitive to allegations of injury to workers from imports, and in particular the charge that through offshore operations U.S. companies are exporting jobs. Every objective study in the past has indicated that the production-sharing enterprises utilizing tariff items 806.30 and 807.00, on balance, actually maintains employment in the United States by making U.S. products involving assembly abroad more cost-competitive with direct imports.

Thus, we find that production-sharing arrangements reduce costs, increase sales and market share, which in turn increase domestic production and employment, or at the least, these arrangements minimize losses in sales and market share, and minimize domestic production declines and job losses.

I would cite our own study entitled "Tariff Items 806.30/807 and Production Sharing, Making U.S. Products More Competitive in the Marketplaces of the World." It is attached as an appendix to this statement, and we have requested that it be included as a part of this hearing record.

There is no requirement for utilizing U.S. components in products manufactured in the Caribbean Basin to be granted duty-free treatment. European or Far Eastern enterprises also might be encouraged to establish manufacturing operations in Caribbean Basin countries to take advantage of the new duty-free access to U.S. markets. The more limited duty-free treatment under the generalized system of preferences has not attracted any significant outside investment to the Caribbean Basin.

The administration's proposal will require that there be a local value added of 25 percent for a product to qualify for the duty-free treatment in contrast to the 35 percent local value added required under GSP. Such a requirement is necessary to avoid "pass through" operations involving mere manipulation of foreign dutiable goods to qualify as a CBI origin product eligible for duty-free treatment.

At the same time, the 25 percent local value added should be the maximum requirement given the basic resource limit on potential local inputs. It is believed that the 25 percent local value added will be sufficent to bar the runaway plant possibility.

The governments of the beneficiary countries have an important responsibility to take steps to assure themselves that the new enterprises attracted by the U.S. free trade area involved processing or manufacturing operations which do result in real benefits locally. Otherwise, the "pass through" possibilities could cause unnecessary objections and trade policy confrontations.

Beyond this, the administration proposal recognizes that the trade created by the free trade area conceivably could have an impact on domestic workers and industries. Given the existing resource base and the size of the economies—$45 billion in gross domestic product and 39 million in population—it does no seem likely that serious injury to domestic producing interests could occur.

However, in the event imports of a magnitude develop that threaten or cause serious injury to a domestic industry, the import relief provisions of U.S. trade law will be applicable. In the case of perishable commodities, emergency import relief could be made available. Since the free trade area is a unilateral action on the part of the United States, the willingness of the U.S. Government to employ temporary relief measures in cases of serious injury to domestic industries caused by such duty-free imports should be understood.

On the basis of our own experience in production-sharing and on the basis of these countries' experience with the generalized system of preferences, the CBI free trade area concept presents U.S. industry and workers with major trade opportunites in the future.

In the attached table 2, imports under item 806.30 and 807.00 are shown, with details for developed and developing countries and for the countries of the Caribbean Basin.

The statistics confirm that in trade involving duty-free treatment for the value of the U.S. materials used in the offshore assembly or processing, the value of the foreign content is a much lower percentage of the import value, 37 percent, than for all less developed countreis, 50 percent, or for developed countries, 93 percent.

These percentages demonstrate the lack of indigenous resources in the Caribbean Basin and the benefits to U.S. companies of production-sharing. That is, 63 percent of the value of imports under tariff items 806.30 and 807.00 from Caribbean Basin countries are U.S. materials.

In utilizing these U.S. components, production-sharing increases employment, adds to the skills of the workers, and contributes to the development of infrastructure so vital to further economic development in beneficiary countries.

These arrangements are active examples of transferring technological know-how to the benefit of both beneficiary countries and production-sharing companies. The whole range of electronic products has labor-intensive operations which lend themselves to production-sharing.

It well may be that the Caribbean Basin free trade area can attract offshore electronic manufacturing operations from the Far East from which direct imports presently pose a continuing competitive thrust to U.S. manufacturers.

Since it is well known that production-sharing enterprises operate in the textile and apparel area, let me anticipate a question. imports of apparel fabricated and assembled abroad and entered under item 807.00 are subject to the bilateral agreement restraints of the textile program even though U.S. textiles almost exclusively are utilized in such offshore operations.

While many of our companies would prefer otherwise, present regulations requires such treatment. Likewise, textile and apparel imports subject to the textile program will not be included in the Caribbean Basin free trade area.

We hope that the U.S. Government's intent, as indicated in presenting the CBI, to allow more favorable access for Cabibbean Basin—textile and apparel—products will be acted upon.

We request this subcommittee, in it favorable report on the CBI legislation, to urge the administration to allow more favorable import access to Caribbean Basin textile and apparel products, particularly in those countries where bilateral agreements already are restraining such trade.

Textile and apparel trade is an important segment of development needs in the Caribbean Basin.

We have primarily addressed ourselves to that part of the Caribbean Basin Initiative to which we are most sensititve, the opportunity for production-sharing which provides for the first two needs of any program of economic development:

First, jobs and developing skills; and second, increasing foreign exchange earnings.

The modest scale of potential development poses no discernible domestic threats, but opportunities for expanded nontraditional exports through production-sharing arrangement.

The other aspects of the program are equal parts of this skillfully integrated program aimed at private initiative self-help. The fragile policical stability in some countries and thus the entire basin make the concessional aid package essential, even without the immediate and pressing economic and financial needs of several countries.

Regarding concessional aid, we note that development assistance is to emphasize agriculture, health and population problems. Agriculture in these economes is a very slow means to development. Under current circumstances, we believe that development and economic support funds should focus on a strategy for developing nontraditional exports, to the extent feasible.

The immediate payoff in increased foreign exchange earnings from nontraditional exports provides earlier overal stimulus to economic development than will the traditional assistance to agriculture activities. A creative approached used in an AID-sponsored project in Costa Rica, BANEX, to finance nontraditional export is a case in point.

The investment climate must be improved if the opportunities presented by the free trade area are to be taken advantage of and if export market potentials in other countries are to be realized.

Thus, the tax measures are necessary incentives to commitments by U.S. investors just as the bilateral investment treaties are commitments by the Caribbean Basin countries to development through creation of the necessary climate for private investment.

However, these nations cannot through their own resources provide the spreading of the risk that the needed investments will require. Thus, the investments and investment insurance of the OPIC programs are a necessary element in the total program of private enterprise development.

The Export-Import Bank, the Inter-American Develoment Bank, and the World Bank hopefully will support joint ventures in their efforts toward development goals.

We urge the subcommittee on trade to favorably report the CBI legislation and, in doing so, to strongly endorse the total integrated program of the CBI. To those of us on the Committee for 806.30 and 807, Inc., it truly represents an endorsement of the concept of the shared benefits of economic development in developing countries through production-sharing.

Mr. Chairman, it will soon be the 50th anniversary of President Roosevelt's Good Neighbor Policy. It has been two decades since President John F. Kennedy proposed the Alliance for Progress. These programs were well-founded in strategic concepts and well-intended in economic terms for forging mutual help and cooperation in the Westen Hemisphere.

The fact is that we can only celebrate their good intentions because the United States did not follow through on the implicit commitments of either plan. Other events in the world and at home seem to get in our way.

You have before you President Reagan's Caribbean Basin Initiative. it addresses the more immediate and pressing concerns in the Western Hemisphere. The United States must make the commitment to carry out this integrated program of trade, aid and investment in the Caribbean Basin, and to follow through on that commitment. Our history requires that we do not again fail to act when our idealism and pragmatism also demand it.

[The prepared statement follows:]

Statement of Cameron Clark, Jr., President of the Committee for 806.30 and 807, Inc.

SUMMARY

The Committee for 806.30 and 807, Inc. strongly supports enactment of the Caribbean Basin Economic Recovery Act. We believe that Administration's Caribbean Basin Initiative (CB) is in the national interest of the United States, strategically, economically, and commercially.

Stategically, the area's importance to the United States demands we take every feasible measure to encourage growth in the context of private initiative and stable, responsive government.

Economically, the program can restore confidence and become an engine for widespread development in the region with long-term benefits for the United States.

Commercially, the development potential of the program lies in nontraditional exports. Such exports can increase needed foreign exchange earnings so essential to the economies of these small countries. Such export-led development can benefit U.S. industries and workers by expanding markets for U.S. exports.

In our companies' operations under tariff items 806.30 and 807.00 we have seen the benefits that production sharing enterprises can bring to these small countries, in terms of increasing employment and incomes, upgrading labor skills, and creating a demand for auxiliary and support services.

On the basis of our own experience in production sharing and on the basis of these countries' experience with GSP, the CBI free trade area concept presents U.S. industry and workers with major trade opportunities in the future.

We request that the Committee's report on this legislation urge the administration to allow more favorable import access to Caribbean textile and apparel products, in accordance with its stated commitments.

The other aspects of the program are equal parts of a skillfully integrated proposal aimed at private intitiative self-help. The concessional aid package is essential and should focus of increasing earnings from nontraditional exports. The improvement in investment climate is necessary if exports potentials are to be realized; thus, the tax measures and bilateral investment treaties are necessary. Investment guarantees, and the investment insurance program of OPIC and other financial institutions will provide needed risk-spreading, plus, hopefully, short-term credit assistance for meaningful private enterprise participation in the development and trading process.

This integrated program is the strongest contribution that the United States can make to the pressing economic and social needs of the Caribbean Basin.

STATEMENT [1]

Mr. Chairman, members of the Subcommittee on Trade: As President of the Committee for 806.30 and 807, Inc., I am privileged to appear before you and strongly endorse the Administration's Caribbean Basin Initiative. I am also President of my own firm, Production Sharing International Ltd., of Southport, Connecticut. With me is Dr. Ralph Biedermann, Vice President of our Committee for 806.30 and 807, Inc., and Director of Corporate Relations for the Brunswick Corporation, Skokie, Illinois.

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[1] The Committee for 806.30 and 807, Inc. is a Washington-based organization which supports the principles of and the need for tariff items 806.30, 807 and production sharing. It was founded in 1976 and is comprised of member firms who operate or support facilities utilizing these tariff provisions. The Committee seeks to communicate the benefits of the use of these provisions to all interested parties, to conduct research on the economic and social impacts which these provisions have on the United States and other countries and to provide a forum for those interested in the production sharing process.

Your Subcommittee's prompt hearing on the Administration's proposal for Central America and the Caribbean area is most commendable, particularly at this time. There is a lack of concensus and a vast amount of confusion in the United States on the appropriate approach to growing political instability in this vital region. In considering this program it must be recognized that the lack of political stability prevents any immediate progress on social problems and on economic development in particular countries. Nevertheless you must not permit the confusion and lack of consensus to postpone action on the Caribbean Basin proposal.

This program of integrated incentives to self-help is the strongest contribution that can be made to the pressing economic and social needs of the Caribbean Basin. It is also in the national interest of the United States, strategically, economically and commercially.

The strategic importance of this region to the security interests of the United States is really not debatable. The stimulus of the trade and investment incentives will contribute to stronger economies in the region with long term economic and political benefits for the United States. Commercially, increased private enterprise participation, an integral part of the program, can mean increased U.S. exports as a larger share of growing markets in the Caribbean Basin.

Our Committee for 806.30 and 807, Inc. has members who already have plants assembling U.S. made components in at least 13 of the more than 20 small nations in Central America and the Caribbean area. As this Subcommittee is aware, these plants process and assemble U.S. materials and components and utilize the special duty provisions of tariff items 806.30 and 807.00 upon return of the articles to the United States. In Central and South America, these assembly operations, for the most part, are designed to employ workers in labor intensive operations. The labor performed in these operations is unavailable in the United States or is not available in quantities and at costs which permit total U.S. manufacture at prices competitive with direct imports into the United States.

In operating these plants in the Caribbean we live with economic, social, and political conditions of the Caribbean Basin. We have become increasingly concerned at the decline in those conditions in recent years. They stand in stark contrast to the potentials for economic progress that could be realized through trade development.

We are very much aware that the great increase in the cost of oil beginning 8 years ago has placed an enormous burden on most of the small economies. As participants in these economies, we are constantly reminded that earnings from traditional exports such as sugar, coffee, and bauxite have fallen. As needed imports have increased in price due to inflation in the industrialized countries, the result for the Caribbean Basin has been crippling balance of payment deficits and dangerously declining international reserves.

Our members daily observe the impact of high levels of inflation in these countries as the workers have to deal with declines in real income. High interest rates and the general lack of credit choke new investment opportunities and discourage economic growth.

These conditions our members see and experience first hand. Thus, we support the Administration's initiative to foster general economic progress and improvement in social conditions in the Caribbean Basin. But the question of political stability cannot be ignored. The strategic importance of the Caribbean-Central American area demands that the United States take every feasible measure to encourage economic growth in the context of private initiative and stable, responsive government.

The expanded access to the United States markets, coupled with the investment incentives through tax inducements, and further assurances of the bilateral investment treaties and investment assistance and insurance through the Overseas Private Investment Corporation, all combine to open up private enterprise opportunities in the Caribbean Basin. With imaginative support of medium-term credit or credit guarantees (possibly to indigenous commercial banks) by the Export Import Bank, the Caribbean Basin Initiative can contribute to a dramatic turnaround in the area's economic decline. In short, this integrated program of self-help, emphasizing the role of private enterprise, provides an umbrella for more effective evolution of relations between the private sectors in the beneficiary countries and in the United States. It can restore confidence and become the engine for widespread economic development in the region.

In this overall effort we have the cooperation of Canada, Mexico, and Venezuela, each country having pledged to continue their own unique economic assistance programs in this area. Our European and Japanese trading partners have expressed support and promised assistance, where appropriate.

In overseas operations under tariff items 806.30 and 807.00, we have also seen the benefits that production sharing enterprises can bring to these small countries, in terms of increasing employment and incomes, upgrading labor skills, and creating a demand for auxiliary and support services.

The free trade area proposed in the Caribbean Basin Initiative would permit all imports from beneficiary countries to enter the U.S. free of duty, except for textiles and apparel articles subject to the Multifiber Arrangement (MFA) and the supporting bilateral agreements on textiles and apparel. The free trade area would be in effect for a period of 12 years—a necessary time requirement to initiate investment plans and realize investment returns.

U.S. imports from the twenty countries and semi-independent island nations were $10 billion in 1981, and of that total, $6 billion were U.S. imports from the Bahamas, Trinidad and Tobago, and the Netherland Antilles, mostly exports of crude petroleum and refined petroleum products. In total, 87 percent of the imports from the Caribbean Basin countries currently are virtually duty-free. It is the potential represented by the 13 percent which makes the free trade area so vital to the countries of the Caribbean Basin.

The potential lies in the nontraditional exports of the traditionally underdeveloped economies, not raw material and tropical products, but manufactures and processed articles—many of which are adaptable to production sharing arrangements. These non-traditional exports can increase needed foreign exchange earnings so essential to the economies of these small countries. Such export-led development can benefit U.S. industries and workers by expanding markets for U.S. exports. Where they are feasible, production sharing arrangements can increase competitive ability of U.S. goods in the domestic market and abroad. Attached to this statement is Table 1, showing total 1981 imports and free and dutiable imports from each country in the Caribbean Basin.

There are two elements of the proposal for the free trade area that must be considered. The Committee for 806.30 and 807, Inc. is very sensitive to allegations of injury to workers from imports, and in particular the charge that through offshore operations U.S. companies are exporting jobs. Every objective study in the past has indicated that the production sharing enterprises utilizing tariff items 806.30 and 807.00, on balance, actually maintains employment in the United States by making U.S. products involving assembly abroad more cost competitive with direct imports. Thus, we find that production sharing arrangements reduce costs, increase sales and market share which in turn increase domestic production and employment, or at the least, these arrangements minimize losses in sales and market share, and minimize domestic production declines and job losses. I would cite our own study, entitled, "Tariff Items 806.30/807 and Production Sharing, Making U.S. Products More Competitive in the Market Places of the World." It is attached as an appendix to this statement, and we have requested that it be included as a part of this hearing record.

There is no requirement for utilizing U.S. components in products manufactured in the Caribbean Basin to be granted duty-free treatment. European or Far Eastern enterprises also might be encouraged to establish manufacturing operations in Caribbean Basin countries to take advantage of the new duty-free access to the U.S. markets. The more limited duty-free treatment under the Generalized System of Preference (GSP) has not attracted any significant outside investment to the Caribbean Basin.

The Administration's proposal will require that there be a local value added of 25 percent for a product to qualify for the duty-free treatment in contrast to the 35 percent local value added required under GSP. Such a requirement is necessary to avoid "pass through" operations involving mere manipulation of foreign dutiable goods to qualify as a CBI origin product eligible for duty-free treatment. At the same time the 25 percent local value added should be the maximum requirement given the basic resource limit on potential local inputs. It is believed that the 25 percent local value added will bar the runaway plant possibility.

The governments of the beneficiary countries have a responsibility to take steps to assure themselves that the new enterprises attracted by the U.S. free trade area involve processing or manufacturing operations which do result in real benefits locally. Otherwise, the "pass through" possibilities could cause unnecessary objections and trade policy confrontations.

Beyond this, the Administration proposal recognizes that the trade created by the free trade area conceivably could have an impact on domestic workers and industries. Given the existing resource base and the size of the economies ($45 billion in gross domestic product and 39 million in population), it does not seem likely that serious injury to domestic producing interests could occur. However, in the event imports of a magnitude develop that threaten or cause serious injury to a domestic industry, the import relief provisions of U.S. trade law will be applicable. In the case of perishable commodities, emergency import relief could be made available. Since the free trade area is a unilateral action on the part of the United States, the willingness of the U.S. Government to employ temporary relief measures in cases of serious injury to domestic industries caused by such duty-free imports should be understood. On the basis of our own experience in production sharing and on the basis of these countries' experiences with the Generalized System of Preferences (GSP), the CBI free trade area concept presents U.S. industry and workers with major trade opportunities in the future.

In the attached Table 2, imports under item 806.30 and 807.00 are shown, with details for developed and developing countries and for the countries of the Caribbean Basin. The statistics confirm that in trade involving duty-free treatment for the value of the U.S. materials used in the offshore assembly or processing, the value of the foreign content is a much lower percentage of the import value, 37 percent, than for all less developed countries, 50 percent, or for developed countries, 93 percent. These percentages both demonstrate the lack of indigenous resources in the Caribbean Basin, and the benefits to United States companies of production sharing. That is, 63 percent of the value of imports under tariff items 806.30 and 807.00 from Caribbean Basin countries are U.S. materials.

In utilizing these U.S. components, production sharing increases employment, adds to the skills of the workers, and contributes to the development of infrastructure so vital to further economic development. These arrangements are active examples of transferring technological know-how to the benefit of both production sharing countries. The whole range of electronic goods has labor intensive operations which lend themselves to production sharing. It well may be that the Caribbean Basin free trade area can attract offshore electronic manufacturing operations from the Far East from which direct imports presently pose a continuing competitive thrust.

Since it is well known that production sharing enterprises operate in the textile and apparel area, let me anticipate a question. Imports of apparel fabricated and assembled abroad and entered under item 807.00 are subject to the bilateral agreement restraints of the textile program even though U.S. textiles amost exclusively are utilized in such offshore operations. While many of our companies would prefer otherwise, present regulations require such treatment. Likewise, textile and apparel imports subject to the textile program will not be included in the Caribbean Basin free trade area. We hope that the U.S. Government's intent, as indicated in presenting the CBI, to allow more favorable access for Caribbean Basin (textile and apparel) products will be acted upon. We request this Subcommittee, in its favorable report on the CBI legislation, to urge the Administration to allow more favorable import access to Caribbean Basin textile and apparel products, particularly in those countries where bilateral agreements already are restraining such trade. Textile and apparel trade is an important segment of development needs in the Caribbean Basin.

We have primarily addressed ourselves to that part of the Caribbean Basin Initiative to which we are most sensitive, the opportunity for production sharing which provides for the first two needs of any program of economic development: first, jobs and developing skills, and second, increasing foreign exchange earnings. The modest scale of potential development poses no discernible domestic threats but opportunities for expanded nontraditional exports through production sharing arrangements.

The other aspects of the program are equal parts of this skillfully integrated program aimed at private initiative self help. The fragile political stability in some countries and thus the entire basin, make the concessional aid package essential, even without the immediate and pressing economic and financial needs of several countries.

Regarding concessional aid, we note that development assistance is to emphasize agricultural, health and population problems. Agriculture in these economies is a very slow means to development. Under current circumstances, we beleve that development and economic support funds should focus on a strategy for developing nontraditional exports, to the extent feasible. The immediate payoff in increased foreign exchange earnings from nontraditional exports provides earlier overall stimulus to economic development than will the traditional assistance to agricultural activites. A creative approach used in an AID sponsored project in Cost Rica (BANEX) to finance non-traditional exports is a case in point.

The investment climate must be improved if the opportunities presented by the free trade area are to be taken advantage of and if export market potentials in other countries are to be realized. Thus, the tax measures are necessary incentives to commitments by U.S. investors just as the bilateral investment treaties are commitments by the Carribean Basin countries to development through creation of the necessary climate for private investment. However, these nations cannot through their own resources provide the spreading of the risk that the needed investment will require. Thus, the investments and investment insurance of the OPIC programs are a necessary element in the total program of private enterprise development. The Export Import Bank, the Inter-American Development Bank, and the World Bank hopefully will support joint ventures in their efforts toward development goals.

We urge the Subcommittee on Trade to favorably report the CBI legislation and, in doing so, to strongly endorse the total, integrated program of the CBI. To those of us on the Committee for 806.30 and 807, Inc., it truly represents an endorsement of the concept of the shared benefits of economic development in developing countries through production sharing.

Mr. Chairman, it will soon be the 50th anniversary of President Roosevelt's Good Neighbor Policy. It has been two decades since President John F. Kennedy proposed the Alliance for Progress. These programs were well-founded in strategic concepts and well-intended in economic terms for forging mutual help and cooperation in the Western Hemisphere. The fact is that we can only celebrate their good intentions because the United States did not follow through on the implicit commitments of either plan. Other events in the world and at home seem to get in our way.

You have before you President Reagan's Caribbean Basin Inititative. It addresses the more immediate and pressing concerns in the Western Hemisphere. This country must make the commitment to carry out this integrated program of trade, aid and investment in the Caribbean Basin, and to follow through on that commitment. Our history requires that we do not again fail to act when our idealism and pragmatism also demand it.

Attachment.

TABLE 1.—U.S. IMPORTS FROM COUNTRIES OF THE CARIBBEAN BASIN, DUTIABLE, DUTY-FREE, AND CALCULATED DUTY AS PERCENT OF DUTIABLE VALUE

[Dollar amounts in millions]

Countries	Total	Duty-free [1]	Dutiable	Calculated duty (percent)
Guatemala	$347	$256	$91	2.3
El Salvador	258	174	84	10.1
Honduras	431	330	101	7.3
Nicaragua	140	104	36	6.8
Costa Rica	365	233	132	11.1
Panama	297	231	66	2.0
Haiti	276	81	195	14.4
Dominican Republic	922	405	517	6.5
Belize	42	28	14	19.7
Bermuda	18	17	1	9.0
Bahamas	1,243	132	[1] 1,111	([2])
Jamaica	357	331	26	21.3
Leeward and Windward Islands	32	19	13	20.6
Barbados	81	20	61	13.0
Trinidad and Tobago	2,215	108	[1] 2,107	([2])
Netherland Antilles	2,599	138	[1] 2,461	([2])
Guyana	104	97	7	19.5
Suriname	179	179		9.5
Total	9,906	2,883	7,023	[3] 8.7

[1] Imports of petroleum and petroleum products, primarily.

[2] Ad valorem equivalent of the duty in less than 0.5 percent.

[3] Excludes trade and calculated duties in petrolem and petroleum products.

Source: U.S. Department of Commerce.

TABLE 2.—U.S. IMPORTS UNDER TARIFF ITEMS 806.30 and 807.00 FROM COUNTRIES OF THE CARIBBEAN BASIN, 1980

[Dollar amounts in millions]

Countries	Total	Duty-free [1]	Dutiable
All countries	$14,000	$3,742	$10,258
Developed countries	7,661	579	7,092
Developing countries	6,339	3,163	3,176
Caribbean Basin countries	503	318	185
Haiti	154	105	49
El Salvador	89	51	38
Dominican Republic	98	66	32
Barbados	48	24	24
Costa Rica	45	30	15
Jamaica	15	10	5
Belize	11	7	4
Honduras	14	10	4
Leeward and Windward Islands	9	3	6
Guyana	3	2	1
Trinidad	1	([2])	([2])
French West Indies	3	2	1
Percent distribution between duty-free and dutiable imports:			
Total All Countries	100	26	74
Developed	100	7	93
Developing	100	50	50
Caribbean Basin	100	63	37

[1] Value of U.S. material and parts sent abroad for processing or assembly.

[2] Duty-free imports 0.7 million and dutiable 0.4 million.

Source: U.S. International Trade Commission.

Tariff Items 806.30/807.00

And Production Sharing

making
U.S. products
more competitive
in the
market places
of the world

Committee for 806.30 and 807.00, Inc.
1611 North Kent Street, Suite 800
Arlington, Virginia 22209 703/527-8968

May 1981

About Tariff Items 806.30/807.00 And Production Sharing

Items 806.30 and 807.00 are provided for in Schedule 8, Part 1, Subpart B of the Tariff Schedules of the United States (TSUS). Under the proper conditions, these Items allow for the duty-free treatment of the value of U.S. materials or components sent abroad for processing or assembly and returned as parts of articles or complete articles. Similar provisions, which exclude the value of components of U.S. origin from the total value of the article for duty purposes, have been incorporated in one form or another in the U.S. tariff statutes since the Tariff Act of 1790. A number of industrialized nations, including the members of the European Economic Community, have similar provisions in their own tariff schedules.

Tariff Items 806.30 and 807.00 are utilized by U.S. firms which have their own facilities overseas as well as by U.S. firms which "contract out" processing and assembly operations to foreign-owned firms. The provisions are also utilized by foreign firms which incorporate U.S. components in their products.

The use, by U.S. firms, of these Tariff Items for processing and assembly operations in conjunction with foreign-based facilities has been termed "production sharing". In this process, U.S. firms and foreign affiliates or contractors share aspects of the production process. The high labor skills and technology available in the United States for development and manufacture of materials and components are combined with the lower cost factors of production necessary in some processing and assembly operations and available in other countries. Jobs are created in both the United States and in the host countries, and host country earnings flow back to the U.S. as increased foreign purchases of American products.

The "bottom line" is that Items 806.30 and 807.00 enhance U.S. production, employment and exports by making our products more competitive in the marketplaces of the world, as well as in the United States.

Summary

Tariff Items 806.30 and 807.00 provide measurable benefits to American consumers, workers, and industries. These provisions, recognized in principle as part of U.S. trade policy since the Tariff Act of 1790, work successfully to improve U.S. competitiveness, enhance the employment of American workers, support U.S. foreign policy interests, and provide American consumers with low-priced alternatives to foreign imports.

A survey of the most important trends in 806.30/807.00 trade reveals:

- **The total value** of 806.30 and 807.00 imports has increased from $0.9 billion in 1966 to $14.0 billion in 1980, accounting in the latter year for 5.8 percent of the total value of U.S. imports for consumption. More importantly, the U.S. content of these imports has increased from 15.4 percent of their total value in 1966 to 26.7 percent in 1980. In dollar terms, U.S. content has grown from $147 million to $3.7 billion during this period. Most of the growth of 806.30/807.00 trade has been associated with Item 807.00 which represented about 98 percent of the total value of combined imports in 1980.

- **The major participants** in 806.30 and 807.00 trade during 1966 were the industrialized countries. In that year, Canada, West Germany and the U.K. accounted for over 75 percent of total imports under the two Items. Overall, developed countries accounted for 94 percent of 806.30/807.00 imports, supplying mainly advanced technology products such as motor vehicles, aircraft/spacecraft, and office machines.

  By 1980, however, developing nations, led by Mexico, Malaysia and Singapore, were responsible for 45 percent of all 806.30/807.00 imports. Developing country production under these Tariff Items is now concentrated in the high growth areas of electronics and textile/apparel.

- **The employment of American workers** has been enhanced, both directly and indirectly, through the utilization of these Tariff Items. In 1966, approximately 5,100 American workers were directly involved in the production of material and components making up the U.S. content of 806.30 and 807.00 articles. By 1980, this figure had increased dramatically to over 74,000 workers. In addition, the number of U.S. workers involved in further processing of 806.30 and 807.00 articles returned to the United States has grown from about 10,200 in 1966 to approximately 149,000 in 1980. Indirect employment has also increased proportionately.

- **The economic benefits** of production sharing have been felt by host country as well as U.S. participants. Item 806.30 and 807.00 operations in host countries have assisted in reducing unemployment and in stimulating business development. Foreign exchange earned by host governments through 806.30 and 807.00 facilities has been returned to the United States in the form of increased purchases of U.S. goods, further benefiting the American economy.

- **The 'Bottom Line'** is that Tariff Items 806.30 and 807.00 enhance U.S. production, employment and exports by making American products more competitive. These provisions continue to be vital to the long-range economic interests and goals of the United States.

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Introduction

Ever since the United States has traded as a nation, some recognition has been given to the exclusion from duty of the value of components of American origin. Such exclusion is currently provided for in Schedule 8, Part 1, Subpart B, of the Tariff Schedules of the United States (TSUS). Specifically, two provisions allow for the duty-free treatment of the value of U.S. materials or components sent abroad for processing (TSUS 806.30) or assembly (TSUS 807.00) and returned to the United States as parts of articles or completed articles. These provisions are utilized by American firms and by foreign firms which use U.S. components in their products.

The total value of articles imported under Items 806.30 and 807.00 has grown from $0.9 billion in 1966 to $14.0 billion in 1980. Imports under these Items in 1980 amounted to 5.8 percent of the total value of U.S. imports for consumption of $241.0 billion. This represents an increase from 3.6 percent of the $25.4 billion value of U.S. imports in 1966. The U.S. content in 806.30 and 807.00 imports has also increased, from 15.4 percent of the total value in 1966 to 26.7 percent in 1980.

The benefits provided by Tariff Items 806.30 and 807.00 are becoming more apparent as time goes on. The growth of the number of jobs in various export and domestic industries, the contribution to the balance of trade in manufactured products, the enhancement of competitiveness in both domestic and overseas markets, and the savings to consumers, are among the contributions which these provisions make to American industry, workers and purchasers. In addition, as a result of the production sharing process, these benefits are shared with other countries who act as hosts for 806.30 and 807.00 operations.

The purpose of this paper will be to discuss these two Tariff Items from a technical and customs perspective, to present the trends in trade of articles utilizing Items 806.30 and 807.00, to describe the positive impact on employment in the United States, and to briefly view the positive contributions which these Items have made to foreign countries which participate in this production sharing concept.

Background

Tariff Items 806.30 and 807.00 are both provided for in the Tariff Schedules of the United States (TSUS). Schedule 8. Part 1. Subpart B. The TSUS had its beginnings in the *Tariff Classification Study* conducted by the United States Tariff Commission, now the International Trade Commission, from 1954 to 1962 to replace the Tariff Act of 1930.[1] The following is a brief description of the technical and customs considerations and the legislative history of these two Items.

Tariff Item 806.30

Pursuant to the provisions of Item 806.30,

> "any article of metal (except precious metal) manufactured in the United States or subjected to a process of manufacture in the United States, if exported for further processing, and if the exported article as processed outside the United States, or the article which results from the processing outside the United States, is returned to the United States for further processing . . . "

shall be assessed" . . . a duty upon the value of such processing outside the United States".[2] With respect to entries under Item 806.30, the rate of duty will be that rate which would apply to the article itself if it were not under the provisions of Section 8.

For articles processed outside the United States under Item 806.30, the form of the base metal article may be changed as long as the article is returned to the United States and is further processed. The U.S. Customs Service has held that melting, machining, grinding, drilling, tapping, threading, cutting, punching, rolling, forming, plating and galvanizing are operations which qualify as "processing" under Item 806.30. Examples of articles subject to duty allowance under this Item are:

- Aluminum sheets processed from ingots of U.S. origin and returned to the United States to be cut to size and shape
- Lead ingots produced from lead scrap of U.S. origin and returned for further processing
- Metal screws made abroad from domestic wire and returned for plating
- Tungsten carbide powder sent abroad for sintering and returned for further processing
- Electronic circuits printed on silicon wafers, exported for splitting and returned

Item 806.30 incorporates into the TSUS without significant change, the provisions of paragraph 1615 (g) of the Tariff Act of 1930 as amended by the Customs Simplification Act of 1956. The provisions in the Customs Simplification Act of 1956, as initially proposed, were intended to facilitate the processing of U.S. metal articles in contiguous areas of Canada during breakdowns or other emergencies at nearby plants in the United States. The language of the provision was broadened by the Senate Finance Committee to include all foreign countries. Item 806.30 has not been amended since it was included in the TSUS.

Tariff Item 807.00

Under the provisions of Item 807.00,

> **"articles assembled abroad in whole or in part of fabricated components, the product of the United States, which (a) were exported in condition ready for assembly without further**

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[1] U.S. Tariff Commission, *Tariff Classification Study*, Washington, D.C., 1960. Several supplemental reports were released through 1962. See in particular the Commission's explanatory notes for Section 8, Part 1.

[2] U.S. International Trade Commission, *Tariff Schedules of the United States Annotated: 1981*, Washington, D.C. 1980, p. 742.

Background, cont'd.

> fabrication, (b) have not lost their physical identity in such articles by change in form, shape, or otherwise, and (c) have not been advanced in value or improved in condition abroad except by being assembled and except by operations incidental to the assembly process such as cleaning, lubricating, and painting . . ."

shall be assessed " . . . a duty upon the full value of the imported article, less the cost or value of such products of the United States." The rate of duty assessed under Item 807.00 is that rate which would apply to the article itself without the presence of Item 807.00. Where the Customs Service determines that the value is not sufficient, normally the computed value as defined in section 402(e) of the Tariff Act of 1930, as amended by the Trade Agreements Act of 1979, is used.

Item 807.00, as noted above, applies only to U.S. fabricated components that are exported ready for assembly and that do not lose their physical appearance or identity in the assembly process. Foreign assembly operations may include sewing, gluing, force-fitting, laminating, crimping, screwing, nailing, riveting, soldering, welding, or the use of fasteners. They may also involve operations incidental to the asembly process such as cleaning, removing rust or grease, applying preservative paint or coating, trimming of filing, placing holes in a component for ease of assembly, and cutting to length of wire, thread or similar products exported in continuous length. Final calibration, testing, marking, sorting, and folding of assembled articles are also incidental to the assembly process. Specific examples of operations allowed under Item 807.00 include:

- Assembly of cut parts of wearing apparel by sewing, hemming or stitching
- Installation of U.S. products on articles of foreign manufacture such as U.S. engines and equipment on foreign-made commercial aircraft
- Assembly of baseball and softball covers and their cores by sewing or stitching
- Assembly of U.S. electrical components by soldering and other operations

Many of the operations currently permissible under Items 806.30 and 807.00 have been so determined through the numerous interpretive decisions of the Customs Court and the Court of Customs and Patent Appeals (recently recreated as the Court of International Trade).

Item 807.00 had no direct counterpart in the Tariff Schedules that existed prior to the effective date of the TSUS of August 31, 1963. It was formulated as part of the *Tariff Classification Study* to place on a sound basis an anomalous but well-established practice arising under paragraph 1615 (a) of the Tariff Act of 1930 as a result of a 1954 decision of the United States Customs Court. Under paragraph 1615 (a) American goods returned to the United States that had not been "advanced in value or improved in condition by any process of manufacture or any other means" could receive duty-free treatment. The Customs Service, in attempting to determine which components should receive duty-free treatment, used a criterion of "constructive segregation" under

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[1] U.S. International Trade Commission, *Tariff Schedules of the United States Annotated: 1981*, Washington, D.C., 1980, p. 742.

Background, cont'd.

which U.S. components had to be capable of being identified and removed without injury. The U.S. Customs Court in 1954 decided that labor expended abroad to assemble U.S. components with other components did not advance the value of the U.S. components. It also found that U.S. components contained in imported articles would qualify for duty-free entry, if such components could be identified as the identical product exported from the United States and as not having been changed in any manner other than their assembly into a new or different article.

In the *Tariff Classification Study*, the Tariff Commission argued that the two prime requirements of Item 807.00 are that U.S. parts have been assembled into imported articles and that these parts were not changed in identity during the assembly process. This intent was incorporated into the original 1963 language of the article description for Item 807.00 in the Tariff Schedules, "articles assembled in whole or in part of products of the United States which were exported for such purposes and which have not been advanced in value or improved in condition by any means other than the act of assembly". This provision was first amended in 1965 by Public Law 89-241 to remove certain ambiguities and to allow minor operations incidental to the assembly process. Further amendments were made in 1966 in Public Law 89-806, which eliminated the requirements that the U.S. component be exported for the purpose of assembly and that there be an intention at the time of exportation that it be returned to the United States. There has been no further legislation on Item 807.00 since 1966.

Trends in Trade

As the importance of international trade in the world economy has increased during the past two decades, American manufacturers have faced growing competition from foreign producers in both domestic and overseas markets. The dollar value of U.S. exports has risen steadily—from approximately $29.5 billion in 1966 to over $181 billion in 1979. However, over the same period, American exports have declined as a share of total world exports from 16.6 percent in 1966 to 12.1 percent in 1979.

In the same time frame, U.S. imports have risen sharply in dollar value. Total U.S. imports have increased from $25.4 billion in 1966 to approximately $206 billion in 1979. In relative terms, the U.S. share of total world imports has remained basically stable at slightly over 14 percent.

The imbalance of relative export decline and import stability has resulted in a U.S. merchandise trade deficit which has ranged from $24.7 to $28.4 billion since 1977. Although the largest portion of this deficit is attributed to the growing costs of imported oil, it is also apparent that U.S. manufactured products are becoming less competitive in both domestic and foreign markets. Department of Commerce figures show that in 1966 the U.S. supplied 20.1 percent of the world's imports of manufactured goods. By 1979, the U.S. share had fallen to 17.4 percent.

Within this overall context of U.S. trade volumes, Item 806.30 and 807.00 transactions are relatively small. However, the significance of production sharing as a method of ensuring the ability of some U.S. industries to remain internationally competitive can not be underestimated. The advantages derived by combining high labor skills and technology available in the U.S. with the lower cost factors of production available in other countries are of particular importance to certain industries which require detailed assembly work. For these industries, U.S. production of components used in 806.30 and 807.00 processing and assembly operations boosts U.S. exports, supports domestic jobs and helps American firms remain price competitive with foreign manufacturers.

Table 1 provides an overview of 806.30 and 807.00 trade in relation to the broader U.S. import position for the period 1966-1980. As illustrated, the share of the value of total U.S. imports represented by combined 806.30/807.00 imports rose from 3.8 percent in 1966 to a high of 6.2 percent in 1973. Since that year, 806.30 and 807.00 imports combined have represented between 5 and 6 percent of total U.S. imports, accounting for 5.8 percent in 1980. In dollar value, the combined total of 806.30/807.00 imports has risen from slightly less than $1 billion to about $14 billion. Throughout the period, imports under 807.00 have been substantially higher than 806.30 imports, accounting for 93 percent of the combined total in 1966 and 98 percent of the total in 1980.

Table 1

U.S. Imports Under Tariff Items 806.30 & 807.00 1966-1980

Year	Total U.S. Imports f.a.s. (Million $'s)	806.30 Imports (Million $'s)	807.00 Imports (Million $'s)	Total 806.30/807.00 Imports (Million $'s)	806.30/807.00 Imports as % of Total U.S. Imports
1966	25,400	63	890	953	3.8
1967	26,700	103	932	1,035	3.9
1968	33,000	122	1.432	1,554	4.7
1969	35,900	193	1,646	1,839	5.1
1970	39,800	204	2.004	2,208	5.5
1971	45,500	199	2,566	2,765	6.0
1972	55,300	318	3.091	3,409	6.2
1973	68,600	463	3,785	4,248	6.2
1974	100,100	544	4,828	5,372	5.4
1975	96,500	455	4,708	5,163	5.4
1976	121,100	474	5,248	5,722	4.7
1977	147,100	465	6,723	7,188	4.9
1978	173,000	398	9,337	9,735	5.6
1979	206,000	378	11.559	11,937	5.8
1980	241,000	237	13,762	13,999	5.8

Source: U.S. Department of Commerce. *Overseas Business Reports: United States Foreign Trade Annual 1973-1979* (OBR 80-23). U.S. Gov't Printing Office, Washington, D.C., July 1980.

U.S. Department of Commerce. *Highlights of U.S. Export and Import Trade: December 1980* (FT-990).

U.S. International Trade Commission. *Import Trends in TSUS Items 806.30 and 807.00* (USITC Publication 1029). Washington, D.C., January 1980.

U.S. International Trade Commission Statistical Services Division, preliminary 1980 update of 806.30 & 807.00 import trends.

Table 2 describes the relationship between the total value of 806.30 and 807.00 imports and the value of their U.S. components. As shown, the value of the U.S. content in 806.30 imports has fluctuated between 50 percent and 67 percent of total value for those items.

Under Item 807.00 however, not only the value of the processing abroad, but also the value of any non-U.S made parts incorporated into the product during assembly is dutiable. Even so, as Table 2 suggests, there has been a clear trend toward an increase in U.S. value in 807.00 imports since 1966. In that year, American components represented only 13 percent of total 807.00 import value. But, by 1980, the U.S. value of these articles had grown to slightly over 26 percent.

Table 2

Value of U.S. Components Contained in Tariff Item 806.30 & 807.00 Imports 1966-1980

	806.30			807.00		
Year	Total Value ($ M)	U.S. Value(a) ($ M)	Percent U.S. Value	Total Value ($ M)	U.S. Value(a) ($ M)	Percent U.S. Value
1966	63	34	54	890	113	13
1967	103	51	50	932	147	16
1968	122	65	53	1,432	226	16
1969	193	103	53	1,646	339	21
1970	204	103	50	2,004	434	22
1971	199	124	62	2,566	536	21
1972	318	[illegible]	59	3,090	680	22
1973	463	250	54	3,784	759	20
1974	544	303	56	4,828	1,009	21
1975	455	262	58	4,707	1,0[illegible]	21
1976	474	275	58	5,247	1,271	24
1977	465	274	59	6,723	1,702	25
1978	398	243	61	9,337	2,348	25
1979	378	213	56	11,559	3,091	27
1980	237	158	67	13,762	3,584	26

Source: U.S. International Trade Commission. *Import Trends in TSUS Items 806.30 and 807.00* (USITC Publication 1029). Washington, D.C., January 1980.

U.S. International Trade Commission Statistical Services Division. preliminary 1980 update of 806.30 & 807.00 import trends.

(a) Dutiable Value may be obtained by deducting U.S. Value from Total Value.

Using the selected years 1966, 1970, 1975, and 1980 to establish a trend, Table 3 indicates the major countries of origin for 806.30 imports. As shown, the developed nations, particularly West Germany, Canada and Belgium are the most important sources of these imports. It is clear, however, that developing nations, especially Mexico and Malaysia, are becoming suppliers of increasing importance.

Table 3

U.S. Imports for Consumption Under Tariff Item 806.30 By Country of Origin Selected Years

Country	**Total Value ($ M)**				**Percent of Total**			
	1966	**1970**	**1975**	**1980**	**1966**	**1970**	**1975**	**1980**
Developed:								
Canada	42.9	101.1	57.6	69.7	68	50	13	29
W. Germany	7.4	9.5	6.7	36.8	12	5	1	16
Belgium & Luxembourg	2.3	17.0	5.9	9.4	4	8	1	4
Japan	1.0	5.2	1.6	3.2	2	3	(a)	1
Italy	1.8	11.7	7.1	3.1	3	6	1	1
Switzerland	1.5	2.1	4.3	2.6	2	1	1	1
Sweden	—	—	0.5	0.8	(a)	(a)	(a)	(a)
Other	6.1	18.0	6.0	2.1	9	9	1	1
Subtotal:	63.0	164.6	89.7	127.7	100	81	20	54
Developing:								
Mexico	—	7.4	105.2	65.1	(a)	4	23	27
Malaysia	—	—	101.2	24.7	(a)	(a)	22	10
Singapore	—	11.4	66.1	12.9	(a)	6	15	5
Philippines	—	—	24.9	3.0	(a)	(a)	5	1
Korea	—	6.6	31.8	1.4	(a)	3	7	1
Hong Kong	—	3.9	10.4	0.9	(a)	2	2	(a)
Brazil	—	0.2	2.5	0.7	(a)	(a)	1	(a)
Other	0.2	9.9	22.8	0.6	(a)	5	5	(a)
Subtotal:	0.2	39.4	364.9	109.3	(a)	19	80	46
Total:	63.2	204.0	454.6	237.0	100	100	100	100

Source: U.S. International Trade Commission Statistical Services Division. *Tariff Items 807.00 and 806.30, U.S. Imports for Consumption. Specified Years 1966-1979* (June 1980) and annual reports for 1966, 1970, and preliminary 1980.

(a) Less than 1 percent of total.

Trends in Trade, cont'd.

Table 4 presents country-of-origin data for 807.00 imports. Although the developed nations still supplied the majority of these imports during 1980, the developing nations have gained ground rapidly. Japan, West Germany and Canada are the major developed country suppliers, while Mexico, Malaysia and Singapore lead the developing country producers. In general, the industrialized countries are responsible for advanced technology product imports with high value added, such as motor vehicles, aircraft/spacecraft and office machines, while developing countries are the primary sources of such items as transistors, semiconductors, radio transmitters/receivers and textile/apparel products.

Table 4

U.S. Imports for Consumption Under Tariff Item 807.00
By Country of Origin
Selected Years

Country	Total Value ($ M)				Percent of Total			
	1966	1970	1975	1980	1966	1970	1975	1980
Developed:								
Japan	42.2	144.8	349.1	3,280.9	5	7	7	24
W. Germany	443.7	762.6	1,277.6	2,146.8	50	38	27	16
Canada	116.0	265.5	453.2	1,162.2	13	13	10	8
Sweden	44.2	88.0	199.0	333.6	5	4	4	2
United Kingdom	112.7	59.3	239.9	217.2	13	3	5	2
France	33.3	14.2	46.8	150.8	4	(b)	1	1
Netherlands	4.3	21.1	17.6	58.8	(b)	1	(b)	(b)
Other	32.6	150.3	227.4	180.0	4	7	5	2
Subtotal:	829.0	1,505.8	2,810.6	7,530.3	93	73	60	55
Developing:								
Mexico	7.0	211.4	914.6	2,276.3	(b)	11	19	17
Malaysia	(b)	(b)	86.5	795.3	(b)	(b)	1	6
Singapore	(b)	20.1	146.9	780.4	(b)	1	3	6
Taiwan	6.6	85.9	263.0	473.7	(b)	4	6	3
Philippines	0.2	6.1	20.7	409.5	(b)	(b)	(b)	3
Hong Kong	41.4	120.5	137.6	457.8	5	6	3	3
Korea	(b)	20.8	80.2	311.2	(b)	1	2	2
Other	5.3	35.2	267.3	764.6	(b)	2	6	6
Subtotal:	60.5	500.0	1,896.8	6,229.2	7	25	40	45
Total: (a)	889.5	2,005.9	4,707.8	13,762.2	100	100	100	100

Source: U.S. International Trade Commission Statistical Services Division. *Tariff Items 807.00 and 806.30. U.S. Imports for Consumption. Specified Years 1966-1979* (June 1980) and annual reports for 1966, 1970, and preliminary 1980.

(a) Totals may not add due to rounding.

(b) Less than 1 percent of total.

In 1966, developing countries were responsible for approximately 7 percent of 807.00 imports and less than 1 percent of 806.30 imports. By 1980, however, developing countries accounted for 45 percent of all 807.00 imports and 46 percent of 806.30 items. Table 5 shows more specifically the increasing importance of developing country participation in 806.30 and 807.00 operations. In 1966, only 6 percent of total 806.30 and 807.00 articles were sourced in developing countries. By 1980, 45 percent of the imports were received from developing countries.

Table 5

Developing Countries and Tariff Items 806.30/807.00
Selected Years

806.30/807.00 Imports	Year			
	1966	1970	1975	1980
Total: ($ M)	953	2,210	5,163	13,999
From Developing Countries: ($ M)	61	539	2,262	6,339
Developing Countries as Percent of Total:	6	24	44	45

Source: Tables 3 and 4.

The increasing participation of developing countries in 806.30 and 807.00 operations is significant since preliminary analysis suggests that developing country revenues from these operations are used to support increased purchases of U.S. goods, particularly those using higher technology. As shown in Table 6, while overall U.S. exports grew by a factor of approximately 7.5 between 1966 and 1980, U.S. exports to most of the major developing country 806.30 and 807.00 participants grew at a significantly faster pace, ranging from a factor of 11.7 for Hong Kong to 59 for Singapore. Although no direct cause-effect relationship can be demonstrated, it is likely that the revenues produced by 806.30 and 807.00 facilities have enabled some of these countries to become larger consumers of U.S. goods.

Table 6

Growth of U.S. Exports to Principal Developing Country 806.30/807.00 Participants
1966-1980

Country	806.30/807.00 (a) Exports ($ M)		Total U.S. Exports ($ M)		Growth Factor in Total U.S. Exports
	1966	1980	1966	1980	
Mexico	3.6	1,186	1,180	15,145	12.8
Malaysia	—	481	46	1,337	29.1
Singapore	—	409	51	3,033	59.4
Taiwan	3.3	108	237	4,337	18.3
Philippines	0.1	253	348	1,999	5.7
Hong Kong	19.1	114	229	2,686	11.7
All Countries:	148.0	3,742	29,490	220,549	7.5

Source: U.S. Department of Commerce, *Overseas Business Reports: United States Foreign Trade Annual*, U.S. Gov't Printing Office, Washington, D.C. Editions from May 1968 to July 1980.

U.S. Department of Commerce, *Highlights of U.S. Export and Import Trade: December 1980* (FT-990).

U.S. International Trade Commission, *Import Trends in TSUS Items 806.30 and 807.00* (USITC Publication 1029), Washington, D.C., January 1980.

U.S. International Trade Commission Statistical Services Division, preliminary 1980 update of 806.30 & 807.00 import trends.

(a) For purposes of this study, "exports" are equal to the value of U.S. components exported and returned under 806.30 & 807.00 provisions in the year indicated.

To identify the industries in which 807.00 tariff provisions have made the strongest contributions, it is useful to consider the 807.00 trade data in more detail. Table 7 provides a breakdown of 807.00 imports by type of commodity. As shown, three types of products—metal products, textiles/apparel, and miscellaneous manufactures—account for over 99 percent of total 807.00 trade. Other commodity categories, including agricultural, lumber and paper, chemical, and ceramic products have consistently been responsible for less than 1 percent of 807.00 trade.

Table 7

U.S. Imports for Consumption Under Tariff Item 807.00 By Selected Commodity Groups Selected Years

	Total Value (a) ($ M)				Percent of Total			
Commodity Group	**1966**	**1970**	**1975**	**1980**	**1966**	**1970**	**1975**	**1980**
Schedule 1 (Agricultural Products)	0.4	1.0	0.6	0.1	(b)	(b)	(b)	(b)
Schedule 2 (Lumber & Paper Products)	0.4	4.2	20.6	61.6	(b)	(b)	(b)	(b)
Schedule 3 (Textile Products)	7.3	43.1	237.8	515.6	1	2	5	4
Schedule 4 (Chemical Products)	0.2	0.2	0.8	2.3	(b)	(b)	(b)	(b)
Schedule 5 (Ceramic Products)	0.7	0.5	3.0	14.2	(b)	(b)	(b)	(b)
Schedule 6 (Metal Products)	867.7	1,851.0	4,173.1	12,484.1	98	92	89	91
Schedule 7 (Misc. Mfg. Products)	13.1	107.0	271.8	684.4	1	5	6	5
Total:	889.7	2,007.0	4,707.8	13,762.2	100	100	100	100

Source: U.S. International Trade Commission Statistical Services Division, *Tariff Items 807.00 and 806.30, U.S. Imports for Consumption, Specified Years 1966-1979* (June 1980) and annual reports for 1966, 1970, and preliminary 1980.

(a) Totals may not add due to rounding.

(b) Less than 1 percent of total.

Within the three most important broad commodity categories, eight specific products are of particular importance: 1) Body supporting garments account for 25 percent of all textile/apparel 807.00 imports, 2) Motor vehicles, semiconductors and parts, television and radio communications equipment, office machines, aircraft, and internal combustion engines account for over 75 percent of all metal products imports, and 3) Watches and clocks account for over 25 percent of miscellaneous manufactured imports. Table 8 illustrates the importance of each of these eight products in relation to their general commodity group.

Table 8

U.S. Imports for Consumption Under Tariff Item 807.00 By Selected Sub-Commodity Selected Years

Commodity Group & Sub-commodity	Total Value ($ M)				Sub-Commodity as % of Commodity Group			
	1966	1970	1975	1980	1966	1970	1975	1980
Schedule 3 (Textile Products)	7.3	43.1	237.8	515.6				
Body Supporting Garments:	2.3	9.9	55.5	131.4	31	23	23	25
Schedule 6 (Metal Products)	867.7	1,850.1	4,173.1	12,484.1				
Motor Vehicles:	494.1	967.2	1,903.8	5,255.6	57	52	46	42
Semiconductors:	31.3	185.1	312.4	2,450.9	4	10	7	20
TV & Radio Communications Equip:	47.5	170.8	524.8	1,158.1	5	9	13	9
Office Machines:	16.1	137.9	230.9	609.8	2	7	6	5
Aircraft:	121.6	33.7	80.5	(a)	14	2	1	(a)
Internal Combustion Engines	11.9	29.7	203.0	28.2	1	2	5	(b)
Schedule 7 (Misc. Mfg. Products)	13.7	107.0	271.8	664.4				
Wetches & Clocks:	—	3.7	73.8	175.4	—	3	27	26

Source: U.S. International Trade Commission Statistical Services Division. *Tariff Items 807.00 and 806.30, U.S. Imports for Consumption, Specified Years 1966-1979* (June 1980), and annual reports for 1966, 1970 and preliminary 1980.

(a) Duties on most civil aircraft products were eliminated by the Trade Agreements Act of 1979 effective January 1, 1980.

(b) Less than 1 percent.

Employment Effects

To calculate the total number of U.S. workers directly involved in trade under Items 806.30 and 807.00, it is necessary to quantify the amount of labor required 1) to produce the U.S. fabricated components or metal articles which are exported, and 2) to further process or assemble the products upon their re-entry into the United States. Additionally, workers are indirectly involved in supplying the initial raw materials and distributing and servicing the finished products.

The direct employment effects can be calculated based on the U.S. value of articles exported and returned under the two Tariff Items. As illustrated in Table 2, the combined U.S. content of 806.30 and 807.00 imports for 1980 totalled $3,742 million. Using calculations based on productivity indices computed for each industry from data provided in the *Annual Survey of Manufactures*, it is estimated that 74,533 American workers were directly involved in the production of the $3.7 billion of U.S. content during that year. This represents a dramatic increase from the involvement of an estimated 5,103 American workers in 1966.[4] Table 9 provides the details of this growth trend for the period 1966-1980.

Additionally, it is estimated that approximately two workers are involved in further processing for every one worker employed in the initial manufacture of articles described above. Therefore, in 1980, a total of 223,599 American workers were directly involved in 806.30 and 807.00 related operations.

Beyond the quantitative additions to U.S. employment which can be attributed to trade under Tariff Items 806.30 and 807.00, there is also a qualitative effect. U.S. jobs involved in the manufacture of 806.30 and 807.00 materials and components almost always require skilled or semi-skilled workers as opposed to the lower skilled laborers required for simple assembly or processing work. Thus, the workers involved in U.S. component manufacturing jobs receive the high pay and benefits which are now being demanded by the American labor force. Since the future growth of American industry in the world economy lies in the increased use of high technologies and increasingly higher labor skills, it is apparent that the 806.30 and 807.00 tariff provisions are fully supportive of this trend.

In the long run, U.S. corporations are able to significantly enhance their competitiveness through the use of Tariff Items 806.30 and 807.00, and, as a result, are able to employ more workers in their U.S. operations than would be possible in the absence of the provisions.

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[4] As part of its 1970 study on Items 806.30 and 807.00, the Tariff Commission surveyed U.S. manufacturers to determine how many workers were directly involved in fabrication of components and metal articles for export. For further information see United States Tariff Commission, *Economic Factors Affecting the Use of Items 807.00 and 806.30 of the Tariff Schedules of the United States* (TC Publication 339), Washington, D.C., September 1970, pp. 155-65.

Employment Effects, cont'd.

The U.S. industries which benefit most directly as a result of the 806.30 and 807.00 provisions are those involved in supplying component parts for foreign assembly and processing operations. As shown in Table 9, in 1980, 55,547 American workers were involved in the metal products industries, 11,030 in the textile/apparel area, and 6,955 in the miscellaneous manufactures area.

Table 9

Domestic Employment Effects of 806.30/807.00 Exports Selected Years

Schedule A Classification	806.30/807.00 Exports (a) ($ M)				U.S. Employment Attributable to 806.30/807.00 Exports (a)			
	1966	1970	1975	1980	1966	1970	1975	1980
Schedule 1: (Agricultural Products)	0.3	0.9	0.3	0.04	(b)	(b)	(b)	(b)
Schedule 2: (Lumber & Paper Products)	0.2	2.2	13.0	43.8	(b)	79	277	931
Schedule 3: (Textile Products)	4.0	27.9	155.2	330.9	236	1,394	5,086	11,030
Schedule 4: (Chemical Products)	—	0.1	0.6	0.8	(b)	(b)	(b)	(b)
Schedule 5: (Ceramic Products)	0.4	0.1	0.8	3.2	(b)	(b)	(b)	70
Schedule 6: (Metal Products)	138.9	455.1	976.1	3,091.8	4,673	13,606	17,537	55,547
Schedule 7: (Misc. Mfg.)	3.9	52.2	119.9	271.2	194	2,178	3,075	6,955
Total:	147.7	538.5	1,265.9	3,741.7	5,103	17,255	25,975	74,533

Source: U.S. Bureau of the Census, *Annual Survey of Manufactures: Industry Profiles*, U.S. Gov't Printing Office, Washington, D.C., 1971 and 1976 Editions.

U.S. International Trade Commission Statistical Services Division, *Tariff Items 807.00 and 806.30, U.S. Imports for Consumption, Specified Years 1966-1979* (June 1980), and annual reports for 1966, 1970 and preliminary 1980.

(a) For purposes of this study, "exports" are equal to the value of U.S. components returned under 806.30/807.00 provisions in the year indicated.

(b) Less than 25 persons.

Employment Effects, cont'd.

Table 10 provides a breakdown of U.S. job creation in terms of specific product areas. The largest number of workers in a single product area . . . over 46,000 in 1980—are suppliers to the semiconductor industry. The production of radio and TV communications equipment, body-supporting garment materials, office machine inputs and clock component industries each involved over 1,000 workers in 1980.

Table 10

Domestic Employment Effects of 806.30/807.00 Exports
Key Industries
Selected Years

	806.30/807.00 Exports (a) ($ M)				U.S. Employment Attributable to 806.30/807.00 Exports (a)			
Industry	**1966**	**1970**	**1975**	**1980**	**1966**	**1970**	**1975**	**1980**
Body Supporting Garments	1.4	6.4	30.3	77.5	68	328	1052	2,691
Internal Combustion Engines (b)	3.2	16.9	20.4	6.5	99	436	308	98
Office Machines	4.1	61.6	74.4	166.0	127	1846	1452	3240
TV & Radio Communications	20.8	63.8	151.1	290.5	1302	2381	3570	6864
Semiconductors (b)	11.6	90.1	291.9	1,580.3	831	5382	8613	46,634
Motor Vehicles (b)	10.3	17.4	34.3	66.7	187	294	342	665
Aircraft (b)	18.5	18.8	48.6	(c)	786	607	968	(c)
Watches & Clocks	—	1.2	33.2	41.5	—	47	876	1095

Source: U.S. Bureau of the Census, *Annual Survey of Manufactures: Industry Profiles*, U.S. Gov't Printing Office, Washington, D.C., 1971 and 1976 Editions.

U.S. International Trade Commission Statistical Services Division, *Tariff Items 807.00 and 806.30, U.S. Imports for Consumption, Specified Years 1966-1979* (June 1980), and annual reports for 1966, 1970 and preliminary 1980.

(a) For purposes of this study, "exports" are equal to the value of U.S. components returned under 806.30/807.00 provisions in the year indicated.

(b) For 1966, Item 806.30 data are not included.

(c) Duties on most civil aircraft products were eliminated by the Trade Agreements Act of 1979 effective January 1, 1980.

The Impact on Developing Countries

Tariff Items 806.30 and 807.00 exist primarily for the benefit of U.S. economic interests. However, the provisions have had significantly beneficial effects in a number of developing countries and have thus become an effective implement of foreign policy in strengthening U.S.-Developing Country relations. The in-bond programs which were established in a number of developing nations in response to the 806.30 and 807.00 tariff provisions have consumed no U.S. foreign aid, but have stimulated the type of development which is supportive of U.S. policy interests.

Four major areas of impact can be identified: 1) Foreign in-bond programs in a number of developing countries have served as vehicles for technological development, encouraging the use of U.S.-produced machinery and equipment and thus increasing the demand for U.S. exports; 2) Chronic unemployment problems have been eased in a number of areas and the accompanying tensions and unrest which can increase societal susceptibility to foreign power influence have been correspondingly reduced; 3) Government and personal incomes in poor countries have increased as a result of revenues generated by in-bond industries and there is evidence that these additional earnings are being used for increased purchases of U.S. goods and services; 4) Finally, the programs have stimulated the creation of new classes of foreign entrepreneurs and workers who have been able to see the strengths of the U.S. free enterprise system first-hand and who are in excellent positions to support the structure of similar systems within their own countries.

In Mexico, for example, assembly and processing plants have been operating under an "in-bond" program since 1966. This program, established primarily to encourage the location of 806.30 and 807.00 processing facilities in Mexico, has been extremely successful in creating employment opportunities for Mexican citizens, and in generating foreign exchange revenues for the Mexican government. Mexico's geographic proximity to the southern U.S., and the cooperative attitude of Mexican government planners have encouraged the registration of approximately 620 maquiladora plants in Mexico, most of which are heavily involved in 806.30 and 807.00 processing operations. To date, the assembly of electrical and electronic machinery, apparatus, accessories, and related articles has been of primary importance, accounting for over 60 percent of all in-bond production in the nation.

Historically, the area along the U.S.-Mexico border has tended to be economically depressed with high unemployment and low per capita income. Tariff Items 806.30 and 807.00, together with the Mexican government's own incentive programs, have provided much needed revitalization in the border area. Modern, new industrial parks have sprung up in numerous border areas, and neighboring cities such as El Paso-Juarez and Brownsville-Matamoros have received a much needed economic boost.

Employment has been stimulated in both the United States and Mexico as a result of the "twin plant" system. This system employs higher skilled U.S. workers in American plants to fabricate components for export and further process the articles upon their return, and em-

The Impact on Developing Countries, cont'd.

ploys workers in Mexican plants to perform low skill assembly tasks at a reduced labor cost. U.S. and Mexican workers have thus benefited from increased job opportunities, and income levels on both sides of the border are rising.

The Mexican government expects continued dynamic growth in its in-bond program. Employment in the industry has already increased from 19,000 in 1966 to over 124,000 in 1980. The value added by in-bond plants has also risen significantly —from $7 million in 1966 to over $700 million in 1978. By 1990 it is estimated that the industry will generate almost $10 billion in foreign exchange revenues for Mexico and will employ between 450,000 and 500,000 workers. Additionally, in-bond plant operations will ensure the continued supply of external financial resources, new technology and foreign market links which are critical to Mexican national development plans.[1]

The vigor of the Mexican in-bond industry has strengthened U.S.-Mexican trade ties and has stimulated increased U.S. employment in component-producing industries. Foreign exchange earnings, generated by in-bond operations, have been used to increase Mexican purchases of U.S. products and thus strengthen U.S. exports. In summary, the Mexican and American governments have found that the in-bond industry—806.30/807.00 relationship has been one of substantial mutual benefit.

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[1] Banamex, *Review of the Economic Situation of Mexico*, July 1979-February 1981 editions.

Comment

This report has shown the expanding benefits which the use of Tariff Items 806.30 and 807.00, through the production sharing process, has generated for U.S. industry, workers and consumers through increased trade, employment and competitiveness. There has been an *increase in direct trade* in 806.30/807.00 articles with both developed and developing countries. The total value imported under these provisions has grown from $0.9 billion to $14.0 billion in the 1966-1980 period. The *value of U.S. components has grown* from 15.4 to 26.7 percent of the total value in the period. In dollar terms, this represents an increase from $147 million to $3.7 billion.

As the value of U.S. components has expanded, the *employment of U.S. workers has been enhanced*, both directly and indirectly. The direct number of American workers engaged in the production of U.S. materials for export has increased from approximately 5,100 to over 74,000 in the 1966-1980 period. Also, additional employment has been created to support the further processing or assembly when articles under 806.30/807.00 are returned to the United States.

The host nations, as well as the United States, have favorably benefited from these provisions. The *utilization of 806.30 and 807.00 supports current U.S. foreign policy interests.* Their use assists in the employment and training of lower and non-skilled labor in foreign nations, especially in the developing countries. The provisions encourage the development of the business enterprise system in nations which have been seeking to utilize their industrialization potential, thereby lessening the need for broad development aid by the United States. Through the foreign exchange earned by countries in 806.30/807.00 operations, the *host nations increase their purchases of American products*, particularly those in the higher technology sectors. This has an additional benefit of *creating additional U.S. export jobs.*

The production sharing concept has allowed American firms to remain in the United States, continuing to utilize their high-skill workers to design, develop and manufacture higher technology components and sharing the processing and assembly of some articles with foreign facilities using lower skill workers at commensurate rates. Through this process, *U.S. manufacturers have been able to maintain or increase their competitiveness* in the marketplaces of the world.

About the Committee

The Committee for 806.30 and 807.00 is a Washington-based organization which supports the principles of and the need for Tariff Items 806.30, 807.00 and production sharing. It was founded in 1976 and is comprised of member firms who operate or support facilities utilizing these tariff provisions. The Committee seeks to communicate the benefits of the use of these provisions to all interested parties, to conduct research on the economic and social impacts which these provisions have on the United States and other countries and to provide a forum for those interested in the production sharing process.

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Additional copies of this booklet are available for $5.00 to members and $10.00 to non-members.

Mr. **Bailey**. There seem to be some contradictions in what you are saying. Won't there be a net loss of jobs in the United States as a result of this policy? We have to be honest about that.

Mr. **Clark**. Mr. Bailey, it is our belief, supported by studies and research that we have performed over the years, that there are individual instances of import-sensitive businesses. That is wherein the short term where they could be hurt. Overall, however, we believe there would be a net gain in employment in the United States under the umbrella of the CBI.

Mr. **Bailey**. Let me ask you about that. If you have the initiative which includes investment opportunities for American firms, aren't you in effect exporting a certain amount of capital and a certain amount of technology? And aren't you providing an investment in that area that will increase, and maybe more so? Is that possible at all? Some of the countries enjoy relations with Europe already.

Mr. **Clark**. Yes. Those economic communities do have access to that market. Unfortunately, the Loma Convention has not encouraged investment of EEC countries in the program, where in contrast the CBI does encourage private sector involvement here in the United States.

Mr. **Bailey**. I can see where it would attract American investment and I can see where it could have a potentially negative impact in Europe.

Mr. **Clark**. This program, in our judgment, could encourage EEC countries or countries in the Orient to do further processing in the Caribbean to have access to the U.S. markets.

Mr. **Bailey**. How much would that benefit in terms of attracting capital? Is that going to benefit some of those what you call developing Eastern countries as opposed to the desired effect of increasing significantly the percentage of investment in Caribbean countries?

For example, would you explain to me why the investment contemplated should be lower in percentage? You have to provide the ITC advantage. I don't understand why, and it is not a trick question. I don't understand why. I missed something somewhere.

Mr. **Biederman**. Are you talking about the 25 percent?

Mr. **Bailey**. What is the reason for that?

Mr. **Biederman**. If you look at imports from the Caribbean Basin under 807, only 37 percent of those imports have been of local content. Now under the GSP program, the local content trigger is 35 percent, and it could be very well that these countries do not have a basic infrastructure and capability right now.

Mr. **Bailey**. That is what we want to do. That is exactly my point. I thought those were the kinds of things we wanted to build. What are we going to do by encouraging a pass-through situation? Are we doing as much for those people as a more comprehensive program could?

Mr. **Biederman**. I don't think in the near term. Let us say they have been running around 35 percent under the 807 program.

I don't see how you can jump that up shortly, in a short period of time.

Mr. **Bailey**. I am not talking about jumping it up. I am talking about changing it. Why do you change it down to 25?

Mr. **Clark**. The 35 percent was under GSP. Under Item 807, there is no trigger level.

Mr. **Bailey**. I understand. I am talking about the Caribbean Basin and the domestic content.

Mr. **Clark**. There has to be a content or there would be pass-through.

Mr. **Bailey**. Why would you lower it?

Mr. **Clark**. Well, presently it can be argued that in some cases it has to be raised.

Mr. **Bailey**. What is the net effect?

Mr. **Clark**. I would not necessarily agree with that. The testimony just prior to ours indicated in the shoe industry that 50 percent of the content of the product is labor.

Mr. **Bailey**. Let me ask you something. Why would it be more of your basic cutting, or maybe what you do under 807, and would you move more of that first step down there, would you be encouraged to do that?

Mr. **Biederman**. I think you have to tailor the types of operations.

Mr. **Bailey**. Tailoring is a good word to us.

Mr. **Biederman**. I would imagine that for operations that require lesser skilled capabilities, that that is where you would start.

Mr. **Bailey**. Then you are admitting, and I respect you for it, that the original question I asked about the loss of American jobs would be realized. There would be a certain displacement there?

Mr. **Clark**. Mr. Bailey, let us back up on this. If we take and isolate one product category we can make a case one way or the other for support, or not support of your contention. In the short term there could be a loss of jobs on a limited basis. However, you must look at the dynamics of what has taken place. We look back over the past 25 or 30 years in this country and we have seen an important evolutionary process take place. At the end of World War II 46 percent of the work force in the United States was categorized by the Bureau of Labor Statistics as unskilled or semiskilled.

We then invested heavily in the educational process in this country with the intent of increasing the potential for an increased standard of living, a better way of life and all of those things that go with a more highly educated society.

By 1974, the unskilled and semiskilled segment of the work force had decreased to about 10 percent of the total work force. It is projected that by 1990, and this is a BLS statistic, that the unskilled and semiskilled pool will be down to 4 percent of the total work force.

Now the kind of jobs that we are talking about are the jobs filled by that pool. They are assembly line workers and sewing machine operators.

Mr. **Bailey**. What is being done? Would any part of this program develop markets for those kinds of superior technology and American items?

Mr. **Clark**. As I stated in my informal remarks, let me take an 807 job. We are creating for the beneficiary country a job with the potentiality of adding new foreign exchange of $4,000 per capita.

Mr. **Bailey**. Mr. Clark, I understand your position, and I don't mean to be disrespectful, but are you aware at the same time that we are asking for this investment tax credit advantage and you are asking for these free trade zones, we are cutting back on the very programs that are supposed to attack structural unemployment in this country?

You are asking for a disproportionate number of these jobs being lost in this country, to have been held by people who haven't been given the opportunities or the skills? They are Americans and they are people and they count, too. We are doing away with those programs and we pledged education and the commitment to education is being cut severely in this country.

At the same time I am supposed to say to people back home that I can justify a trade policy of this sort. It doesn't come up as being fair.

You mentioned that unskilled portion. Well, what about our black citizens who are moving into the middle class in this country, hopefully more rapidly, and maybe we can do some more things and change the policies of this Government to enable them to move a little more rapidly. We are not giving people skilled training and we are not helping them respond to changes.

You are talking about building up people down there for political purposes and that is fine, and we have political purposes here, too. If there was some kind of an offset or appreciation policy of this sort, that is fine.

We sit in the subcommittee and we get a request from the administration to zero out trade assistance programs and thanks to the chairman we were able to work out a compromise to keep some of that training.

I am a politician with a responsibility to represent people, and you can tell me how I justify it? You mean in the long run they will die off?

Mr. **Clark**. We have a serious inner-city problem in this country. We have structural unemployment. I am a supporter personally and I don't know about the committee, but I am a supporter of the enterprise zone prospect which President Reagan announced yesterday. This would address some of those problems.

In the United States, we have to look at it from different points of view to get at the core of the problem and the core of the opportunity. The United States in the next 20 years cannot survive without a viable Caribbean Basin region. I have seen the transition from the early days in the development of Puerto Rico in World War II, to the chaos and crisis that exists today in Central America.

Had we back in the days of the Alliance for Progress made the kind of commitments to move for regional economic development, both sides of the question would have been much more satisfied today.

My own complaint about the Caribbean Basin Initiative is that it may be too late and it is something we should have started earlier.

Mr. **Bailey**. Well, Puerto Rico is a part of this country, but do you pay the minimum wage to these people?

Mr. **Clark**. Puerto Rico is on the minimum wage.

Mr. **Bailey**. Do you have plants in other Caribbean countries?

Mr. **Clark**. I have offices in a number of those countries for my business.

Mr. **Bailey**. You don't have any factories?

Mr. **Clark**. No. However, I was President of a Fortune 500 company which was responsible for placing six factories offshore under 807.

Mr. **Bailey**. What countries?

Mr. **Clark**. Mexico, the Dominican Republic, Honduras, and Costa Rica.

Mr. **Bailey**. What are the wages paid there?

Mr. **Clark**. Today in Costa Rica, because of the recent tragic devaluation when the colon went from 8 to 43, the wage today is 66 cents an hour with fringes. It was only a short time ago up around $1.30 or $1.40.

Mr. **Bailey**. What are the fringes?

Mr. **Clark**. The fringes are 39 percent.

Mr. **Bailey**. Do they love the company there?

Mr. **Clark**. Yes, very much.

Mr. **Bailey**. Do they have a union at all?

Mr. **Clark**. They have unions, yes. Most of these countries have unions.

Mr. **Bailey**. How long do the contracts go?

Mr. **Clark**. The terms of the contract, it depends upon the country.

Mr. **Bailey**. What are the collective bargaining laws?

Mr. **Clark**. Some of them are nationally organized unions. In most instances you have to have a union, and under the labor laws in some instances——

Mr. **Bailey**. What was your rate 5 years ago? What were you paying in Costa Rica 5 years ago?

Mr. **Clark**. About 55 cents with fringes, or 60 cents. It went up to about as high as $1.40 and then they have had this trouble.

Mr. **Bailey**. I want to be very fair. What has inflation been in that country in the last 5 years?

Mr. **Clark**. About 15 or 20 percent. I am guessing and I am not absolutely certain.

Mr. **Bailey**. How would the devaluation issue affect that? What has their real increase been, do you know?

Mr. **Clark**. I would say today, it has been a net loss with the devaluation.

Mr. **Bailey**. A net loss?

Mr. **Clark**. Yes.

Mr. **Bailey**. I thank you, Mr. Chairman.

Mr. **Jenkins**. I want to thank you for your testimony. I understand we may have some differences in certain areas, but I appreciate your testimony very much. I understand that those members who take advantage of the 806 and 807, those are your members?

Mr. **Clark**. Yes.

Mr. **Jenkins**. How many members do you have in your association?

Mr. **Clark**. At the last count, it is slightly in excess of 200.

Mr. **Jenkins**. Are most of those in the apparel field?

Mr. **Clark**. No, I would say apparel represents no more than 20 percent of the members.

Mr. **Jenkins**. The advantage that your members might have and thereby creating jobs to some extent is that the component parts made in this country that are assembled in other countries, then enter this country duty free, is that basically correct?

Mr. **Clark**. They are duty free except for the value added.

Mr. **Jenkins**. So to that extent your members would have some advantage over an item manufactured totally in a foreign country. Is that correct?

Mr. **Clark**. It depends on the item. Just to give you a relative comparison, we made a quick analysis here several years ago, and these figures would have to be updated to current conditions, but take an apparel item made in the United States of $13 a dozen, and made in the United States with a total U.S. component. Made in the Orient of Hong Kong or Japanese fabrics, it was somewhere in the neighborhood of $8 or $9 a dozen. Made under item 807, with 50 percent of the product being U.S. value and 50 percent value added abroad, the product price is competitive with the product from the Orient.

As a matter of fact, there are modest advantages. So the net gain from the United States of the companies producing those products, they had the option of either going to Hong Kong or Korea or Taiwan and buying the whole package or they had the option of utilizing U.S. materials and cutting them in the United States and using labor in Honduras or the Dominican Republic, thereby protecting the higher skilled jobs here in the United States.

Mr. **Jenkins**. So to that extent there are some advantages as you indicated to U.S. jobs.

Mr. **Clark**. It is very clear, our study has shown that.

Mr. **Jenkins**. In that regard should not there be some greater advantage for those manufactured items that have a larger component portion made in this country? The question I am asking is: If you have 20 percent component parts, what is wrong with saying that a duty will be a certain rate, but if you have 50 percent U.S. component parts you get a smaller duty, given a further break?

Mr. **Biederman**. Are you saying that the duty should be tied to the amount of U.S. content?

Mr. **Jenkins**. Yes, I am asking that question.

Mr. **Clark**. It depends upon what the objective of such a program would be.

Mr. **Jenkins**. The objective would be to create more U.S. jobs.

Mr. **Clark**. It is our belief that the strategy you suggest is not going to create more U.S. jobs. The bottom line, a manufacturer of a product in any market can only survive as long as he is cost competitive. The manipulation of tariff duties to try to protect that is only going to be a short-term bandaid. Over a period of time it is not going to happen.

In the United States, when I went to work for the Fortune 500 companies, that is back 30 years, they had 2,500 sewing machine operators in Bridgeport, Conn. Those were plants that shifted within a few years after my arrival to New York State. After 4 or 5 years of being in New York, they moved to Alabama and places down south. The only reason those moves were made was that these products had to be cost competitive in the market. That was migration within the United States.

Maybe there should have been legislation back then that said that if you are once in a city you have to stay there forever. I don't think that that would be a very good construction situation. The process of industrial migration has been going on for centuries, and it will go on for centuries to come.

The low end of the industrial ladder and which represents the apparel and shoes and certain electronics, these jobs are going to migrate where the lowest labor costs are. Otherwise those products are not going to be competitive in the market. They are replaced, unfortunately not in your town which has one plant, but they are going to be replaced by the development of higher technology within the industry. We will not be able to trade with Caribbean countries unless they have foreign exchange.

Bananas, sugar, and coffee are not going to be enough to provide economic development for beneficiary countries. That doesn't cover their oil bill right now. We have to share the industrialization process, and I think this is the big Third World question today as to what extent are the developed countries of the world prepared to share the wealth they have been able to generate through the industrialization process.

Can we continue those benefits to our world alone? I do not think so and the committee does not think so. We think we have in the Caribbean Basin Initiative an excellent opportunity to test some of these trade barriers, the breakdown of trade barrier concepts that have been important. CBI is a very, very limited program in the impact because of the population. You are only talking about a region of 39 million people.

Mr. **JENKINS**. Are most of your members located in the Caribbean area?

Mr. **CLARK**. Yes, and I would say 45 percent of our members are doing business in Mexico.

Mr. **JENKINS**. You indicated in your testimony a few minutes ago that you understood that there were politically sensitive areas. You mentioned textiles and shoes and so forth, which obviously is true.

What do you propose, or does your association support trade adjustment relief for displaced employees?

Mr. **CLARK**. Yes.

Mr. **JENKINS**. So you disagree with the administration on that, when they won't ask it be eliminated?

Mr. **CLARK**. We support it, but it isn't as effective as it could be, or I think as it was intended. We support the basic concept if it leads to retraining. If it is just an assistance, as a handout, I wouldn't say we would favor it, but if we retrain them then we would support it.

Mr. **JENKINS**. You would support an appropriation to retrain people who are displaced?

Mr. **CLARK**. I think this is the responsibility of the industry which it has to share. I have been personally a long-time believer if industry creates a problem by their process of migration, that it should assume some of the social responsibilities for retraining what is left.

Mr. **JENKINS**. Thank you for your testimony.

Mr. **VANDER JAGT**. Thank you, Mr. Chairman.

Thank you, Mr. Clark, for your testimony, and Mr. Biederman for being here. I think your contentions in 806 and 807 are that by taking the component parts that are manufactured here and then assembling them where the cost of labor is cheaper and sent back here, enables us at least in some items to be competitive or we would otherwise not be competitive.

Mr. CLARK. That is right.

Mr. VANDER JAGT. So to that extent we are saving jobs here.

Mr. CLARK. That is right.

Mr. VANDER JAGT. The alternative in some instances where we simply can't be competitive, would be to move the whole operation to some other country entirely and we would lose jobs.

Mr. CLARK. And that has been done.

Mr. VANDER JAGT. So there is an alternative to the exporting of jobs.

Mr. CLARK. Yes.

Mr. VANDER JAGT. When an 807 company creates a job in a Caribbean nation, does that trigger the creation of other jobs?

Mr. CLARK. Our studies show that each primary job contributes two secondary jobs, at least two secondary jobs.

Mr. VANDER JAGT. So then we are talking about a total of creating three jobs. What happens to the additional purchasing power of those three people working who would otherwise not be working? What happens to them?

Mr. CLARK. Well, you have an inflow through the value added process, we have estimated of about $4,000 per primary job. That filters down in various ways and it goes to support some of the secondary jobs and it goes to provide foreign exchange to increase the net reserves of a country.

So there are two things. It enables a country to broaden its employment base and it provides opportunity for it to trade in areas where it had not been able to trade before.

Mr. VANDER JAGT. So you are increasing the capacity of that country to spend some of that money and of buying additional other items from the United States, is that correct?

Mr. CLARK. That is correct.

Mr. VANDER JAGT. So in essence you are aiding jobs here.

I thank you very much for your testimony.

Chairman GIBBONS. At Mr. Bailey's request, if we have time today, we will hear from Alfred Rochie, chairman of the TII in Puerto Rico. I would say, Mr. Rochie, if we don't get to you today we will try to get to you tomorrow.

The next set of witnesses is a Legislative Assembly panel of the Commonwealth of Puerto Rico. They are accompanied by other people who may be called upon. That is Mr. Colberg, Mr. Peña Clos, Mr. Ramirez, Mr. Millman, and Dr. Epstein.

Gentlemen, we welcome you and we appreciate your coming all the way from Puerto Rico to give us your views of the problems this legislation has. We would be delighted to hear from you. Thank you.

STATEMENTS OF HON. SEVERO E. COLBERG, SPEAKER OF THE HOUSE, AND HON. SERGIO PEÑA CLOS, ACTING PRESIDENT OF THE SENATE, LEGISLATIVE ASSEMBLY OF PUERTO RICO, ACCOMPANIED BY MARCOS A. RAMÍREZ, SPECIAL COUNSEL, RICHARD M. MILLMAN, WASHINGTON COUNSEL, AND BARBARA EPSTEIN OF HORACE J. DePODWIN ASSOCIATES, INC., ECONOMIC CONSULTANTS TO THE LEGISLATIVE ASSEMBLY

Mr. Colberg. Mr. Chairman, distinguished members of this committee, my name is Severo Colberg, the speaker of the House of Representatives of Puerto Rico's Legislative Assembly. Accompanying me here today is the acting president of the Senate, Mr. Sergio Peña Clos.

The senate president, Miguel Hernández Agosto, would have been here, but recent surgery prevents his attendance.

I am also accompanied by assistants including a representative of the economic consulting firm which the legislative assembly engaged to assist it in its deliberations with respect to the President's proposal known as the Caribbean Basin Initiative.

Yesterday, the Resident Commissioner of Puerto Rico, the Honorable Baltazar Corrada del Rio, asked this committee to, in effect, discount our testimony. Mr. Corrada said we were coming here to talk of the status of Puerto Rico.

Mr. Chairman, this is not correct. We are here to talk about the eocnomic survival of 3.5 million American citizens. We came here to urge you to promote the economic development of the Caribbean—but not by sacrificing the economic development of Puerto Rico.

Mr. Chairman, Puerto Rico wants to be a partner, not a victim of the Caribbean Basin Initiative.

In a nutshell, as proposed by the President, CBI will strip Puerto Rico of the relative economic advantages of being part of the United States. Puerto Rico's industrial and agricultural products will become noncompetitive not only in the U.S. market, but in Puerto Rico's own markets.

We believe we do not exaggerate when we state that at stake is the economic survival of our island.

For the people of Puerto Rico, the CBI proposal represents an historical moment in Puerto Rico's 84-year relationship with the United States. I state this authoritatively as I, along with Senator Peña Clos, have just presided over 8 days of hearings by a joint committee of the Legislative Assembly of Puerto Rico during which we heard testimony from all sectors of the island's economy as well as testimony from professors of economics and from the political leaders of the island and its former governors.

The record of these proceedings contains extensive testimony which we present to this committee for consideration during its deliberations.

Included, also, is the report of our economic consultant summarizing the economic testimony. At the conclusion of the hearing, conducted by six senators and eight representatives, there was full legislative debate by both bodies of our legislative assembly, resulting in the adoption of a resolution which I am also submitting as part of the record. I feel completely confident in saying that my presentation here today reflects the claims of the broadest based consensus of our people.

Before turning to the conclusions developed, a word about the Puerto Rican Legislative Assembly is in order. History teaches that on issues of magnitude, such as the instant one, it is the legislative assembly that is authorized to represent the claims of the people of Puerto Rico, after full and complete hearing from the people. We note and take exception to the statement of President Reagan that he had "consulted closely with Puerto Rico * * * about the Caribbean Basin Initiative." No such consultation has taken place in accordance with the traditions of Puerto Rico.

The Legislative Assembly of Puerto Rico has reached four conclusions:

First. The legislation which President Reagan submitted, despite the President's statement, does not benefit the economy of Puerto Rico. To the contrary, it will cause extreme and irreversible damage to our economy.

Second. The initiative, both because it does such violence to our economy and because of the manner in which it was developed, namely without appropriate consultation with the people of Puerto Rico, eventually will destabilize the political situation in Puerto Rico.

Third. Puerto Rico is an integral part of the Caribbean Basin. To the extent Puerto Rico prospers, the entire Caribbean Basin and the political initiative of the United States prospers. The contrary is also true; namely, that if Puerto Rico suffers, then the initiative fails and becomes the instrument by which meaningful U.S. bilateral relationships within the Caribbean Basin will be shattered.

Fourth. Affirmative measures must be taken with respect to Puerto Rico if the President's goal that Puerto Rico "benefit and prosper" from the Caribbean Basin Initiative is to be realized.

With respect to my first point; namely, the severe adverse impact CBI causes to our economy, we must start with a recognition that Puerto Rico's problems are not cyclical, but rather are structural. Investment is declining; savings is negative; official unemployment is 22 percent; 40 percent of our youth between 16 and 25 years of age is without work and faces the future with no prospect of finding work. In a word, Puerto Rico is in a depression from which it cannot escape absent structural changes in its economy.

When the CBI and its impact on Puerto Rico are evaluated in light of these facts, the conclusion is inescapable: CBI does not benefit Puerto Rico.

To start with, Puerto Rico already is at a disadvantage in competing with Caribbean countries. The causes are beyond its control. Caribbean countries pay wages that are but a fraction of the minimum wage required to be paid in Puerto Rico; they are unfettered by U.S. legislation such as the Environmental Protection Act and OSHA; by virtue of the San Jose agreement, their petroleum costs 30 percent less than the world market price paid by Puerto Rico; their shipping is not bound by the Jones Act and hence costs less.

Presently, U.S. import duties on products from the Caribbean offset these disadvantages. However, President Reagan proposes to eliminate import duties and give Caribbean countries free access to U.S. markets, including Puerto Rico. This free access combined with a minimal requirement for local Caribbean content will be an incentive for United States, European, and Japanese firms to invest in the Caribbean.

Further, the President proposes to provide added attraction for U.S. investment in Caribbean Basin nations through tax incentives, political risk insurance, and the backing of the U.S. Government.

The net result will be a loss of jobs and industry in Puerto Rico. First, indigenous Caribbean products will replace Puerto Rican products in mainland markets and, more importantly, in Puerto Rican markets.

Next, American firms will be encouraged to move their labor-intensive Puerto Rican operations to low wage Caribbean countries.

And finally, products from Puerto Rico will be placed in direct competition with Japanese and European products which also will gain duty-free access to U.S. markets by the simple process of shifting assembly operations to the Caribbean.

Let me now turn to my second point, namely, the destabilization of Puerto Rico. Is there anyone here that cannot foresee that the inevitable result which CBI will rain on Puerto Rico will be the social and political chaos that inevitably accompanies unemployment, poverty, and the inability to provide for one's own needs and the needs of one's family?

Eventually, unable to export its products, Puerto Rico will be forced to export its most valuable resources, its people.

My third point is that the success or failure of the U.S. political initiative, which is really what CBI is, is inexorably tied to the fate of Puerto Rico under CBI. Unlike mainland States, Puerto Rico is and, what is more important in political terms, is perceived to be still developing.

Moreover, Puerto Rico's economic fate in its relationship with the United States will be a benchmark by which other developing countries will assess the United States. Perhaps the point is best made in a statement by Senator Cranston delivered on the floor of the U.S. Senate on April 2, 1981. Speaking on the proposed budget cuts for Puerto Rico, he stated:

> * * * there is a foreign policy issue and, indeed, a national security issue involved in this matter. There is now great emphasis on our interest in stability and in maintaining and developing friendships in the Caribbean, in Central America where there is the conflict in El Salvador, and in Latin America generally.
>
> If we show total disregard for the people of Puerto Rico, if we permit many Puerto Ricans to slide into even deeper poverty than they presently suffer, and conceivably contribute to economic and social turmoil on that island, plainly this will be very damaging to our national security interests in the Caribbean, Central America and Latin America.
>
> We should do all that we can to make a showcase of democracy and the free enterprise system in Puerto Rico. We should do all we can to make a vivid contrast on that island as against the situation in Cuba and other nations where the people are under Marxist or other systems. It would be a great disservice to our national interest to not understand the needs of Puerto Rico, not take them into account, and not act in accordance with those needs.

Let me now turn to my fourth point, affirmative measures for Puerto Rico as set forth in the resolution of the Legislative Assembly of Puerto Rico.

Congress, in its deliberations, must keep in mind the fact that the economy of Puerto Rico is closer to that of the Caribbean Basin nations than to any of the mainland States. The measures we require must be legislated to assure that Puerto Rico has the same economic opportunities as are contemplated for the Caribbean. We want to be partners in and not victims of the CBI.

The measures we seek are as follows:

One. Assure that Puerto Rico can control imports into its market.

Two. Recognize Puerto Rico's power to enter into internatonal agreements, such as the San Jose agreement, as well as to enter into bilateral and multilateral commercial agreements.

Three. Reduce the cost of shipping goods to and from Puerto Rico which is 1,800 miles from the mainland.

Four. Free our tourist industry from noncompetitive restrictions, for example, the 24-hour limitation on cruise ships visiting Puerto Rico.

Five. Assure that selected products which are vital to the Puerto Rican economy are exempt from trade concessions before Puerto Rican industry is injured.

Finally, Congress must recognize that, as in the case of the other Caribbean countries, the 3.5 million American citizens in Puerto Rico also require direct assistance for economic development. In this regard, we support the proposal being circulated by economists in the Department of Commerce to provide Puerto Rico with a block grant to be used for economic development.

Before concluding my remarks, I would like to quote paragraph 3 of the concurrent resolution passed by the Legislative Assembly of Puerto Rico on March 21, 1982, in response to the proposed Caribbean Basin Initiative:

> This Resolution represents the urgent effort of the Legislative Assembly of Puerto Rico to defend the interests of Puerto Rico and to claim the rights and powers that belong to the people of Puerto Rico, within the framework of the problems aggravated by the Caribbean Basin Initiative. The Legislative Assembly understands that this effort represents only the first step in discussion of the problem and it proposes to initiate a process of consultation among the political sectors of the Puerto Rican community, to reach a consensus on the basic aspects of procedure that will permit the people of Puerto Rico to present to Congress and to the President of the United States an expression of the will of the people of Puerto Rico concerning the political, social, and economic relations between the people of the United States and the people of Puerto Rico.

Puerto Ricans have always demonstrated their loyalty to the United States and supported its policies. We trust that Congress will make it possible for Puerto Rico to wholeheartedly continue in its partnership with the United States.

Mr. Chairman, the supporting documents have been submitted for the record.

[Attachments to the prepared statement follow:]

COMMONWEALTH OF PUERTO RICO
LEGISLATIVE ASSEMBLY
CAPITOL
SAN JUAN, PUERTO RICO 00901

COMO HA PASADO
EN LA CAMARA

9th Legislature 2nd Ordinary Session

HOUSE OF REPRESENTATIVES

H. C. R. 22

March 21, 1982

Introduced by Representatives Colberg-Ramírez, Santiago-García, Jarabo, Acevedo-Lazzarini, Arrarás, Calero-Bermúdez, Carmona-Rivera, Cepeda-García, Coca-Navas, Corujo-Collazo, Figueroa-Hernández, González-Cruz, Jiménez-Meléndez, López-Galarza, López-Hernández, Muñoz-Arjona, Peña-Quiñones, Pérez-Rivera, Ramírez, Rosa-Guzmán, Rosado-Báez, Soriano-González, Tirado-Delgado, Torres-Santiago, Mme. Vélez-de Acevedo, and Mr. Zayas-Bonilla.

Referred to the Committees on Government
and on Constitutional Revision

"CONCURRENT RESOLUTION

To express the sense of the Legislature of the Commonwealth of Puerto Rico on President Reagan's Caribbean Basin Initiative; to petition the President and the Congress of the United States for the approval of certain measures for the benefit and prosperity of Puerto Rico; and to claim recognition by the President and the Congress of the United States of certain rights and powers of the People of Puerto Rico.

STATEMENT OF MOTIVES

WHEREAS: On February 24, 1982, the President of the United States announced his program for the Caribbean before the Organization of American States in Washington, D. C. and made public its contents under the title "Contents of the Caribbean Basin Initiative". The key points of the program consist of granting one-way free trade to the countries of the Caribbean and stimulating, by means of tax and other incentives, the investment of U. S. funds in these countries;

WHEREAS: The sixth point in the President's program reads as follows: "Sixth, given our special, valued, relationship with Puerto Rico and the U. S. Virgin Islands, we will propose special measures to ensure that they also will benefit and prosper from this program. With their strong traditions of democracy and free-enterprise, they can play leading roles in the development of the area."

WHEREAS: The President included in his program a series of measures intended to offset and compensate for the possible negative effects on Puerto Rico of the Caribbean Initiative and to improve Puerto Rico's economy and make it prosper;

WHEREAS: The Governor of Puerto Rico, Carlos Romero-Barceló; the President of the Senate of Puerto Rico, Miguel Hernández Agosto; the Mayor of San Juan, Hernán Padilla, each presented to the administration a series of concrete measures aimed at effectively offsetting the possible negative effects of the Caribbean Initiative and to improve the Puerto Rican economy and make it prosper;

WHEREAS: The representatives of the Executive and Legislative powers of Puerto Rico submitted to the administration more than 25 substantial measures to be included as part of the Caribbean Initiative, with the purpose of offsetting the negative effects of the Initiative and of improving the economy of Puerto Rico; and the administration rejected all but one substantial measure, which extended additional tax benefits to investments in Puerto Rico. It offered to consider other less significant measures;

WHEREAS: On March 4, 1982 both chambers of the Legislature of Puerto Rico approved resolutions creating a Special Joint Committee to study the impact of the Caribbean Initiative on the economic, social, and political life of the Puerto Rican people, through testimony of the Puerto Rican community before the Committe, as represented by economists, farmers, industrial executives, labor leaders, teachers, the presidents of all political parties and former governors of Puerto Rico, religious leaders and other interested citizens;

WHEREAS: The Special Joint Committee, on the basis of public hearings and other information, has arrived at the following conclusions:

1. The economy of Puerto Rico at present is depressed and structurally weak, as reflected in these economic indicators:
    a) chronic unemployment, at about 20 percent.
    b) over 40 percent of young people, between 16 and 24 years of age, is unable to find work;
    c) negative rate of personal savings;
    d) declining private investment in plant and equipment relative to net product; and
    e) virtual standstill in the construction activity.

2. When the reduction in federal funds takes full effect, it will worsen the present economic situation substantially.
3. The one-way free trade arrangement provided for in the Caribbean Initiative will have a severe and adverse effect on the most vulnerable sectors of the Puerto Rican economy: those employing the majority of workers, particularly, agriculture, food processing and the manufacture of selected electric and electronic products.
4. The combination of a weak economic condition with the reduction in federal funds not only will prevent offsetting the adverse effects of the Caribbean Initiative, but will render impossible the long range restructuring and development of our economy.
5. The measures proposed by the President for Puerto Rico are insufficient to offset the adverse effect of the trade concessions and incentives granted to Puerto Rico's Caribbean neighbors.
6. The measure proposed for Puerto Rico in the Caribbean Basin Initiative offer no prospect of promoting the prosperity and development of the economy of Puerto Rico.

7. In summary, the Caribbean Initiative will represent a setback in the development of Puerto Rico's economy which will increase unemployment, paralyze industrial development, destroy agricultural production, weaken the Puerto Rican labor movement, and provoke frustration and unrest among unemployed youths in Puerto Rico. The clearly-predictable result wil be the chaos and social and political instability that inevitably accompany extreme poverty, and the resulting inability of the poor to provide for their needs and those of their families.

8. Although Puerto Rico is in a stage of economic development which is more advanced than the countries benefitted by the Caribbean Initiative, unlike the United States, Puerto Rico is still a developing country which needs the power to control imports to its markets while its local industry develops and becomes more efficient. Puerto Rico's competitors in the Caribbean have this power, while Puerto Rico lacks it.

WHEREAS The public hearings held by this Legislature for the study of the Caribbean Initiative revealed that there is a large measure of consensus and basic agreement between the different political, economic and social sectors of the Puerto Rican Community. The requests for measures and the claims of rights and powers which this Resolution presents to the President and the Congress of the United States are based on these basic agreements and consensus.

WHEREAS: The Legislature of Puerto Rico takes exception to President Reagan's statement that he has consulted Puerto Rico. The Federal Administration's consultation has been with officials of the Executive and Legislative Branches of Puerto Rico, so that the latter could present comments and suggestions to the original proposal. With regard to the recommendations of the Honorable Governor Carlos Romero-Barceló, the Honorable Mayor, Hernán Padilla and the Honorable President of the Senate, Miguel Hernández-Agosto, the Puerto Rican community has had no opportunity to become acquainted with them and express their opinions. The only attempt at public discussion of the problems that the Caribbean Initiative raises for Puerto Rico have been the public hearings and the discussion promoted by this Legislature.

WHEREAS: The Legislature, faithful to its historical and legal tradition of acting as Spokesman for the People of Puerto Rico before the People and the Congress of the United States must exercise its responsibility of bringing before the President and the Congress of the United States, Puerto Rico's claims concerning the threat to its political, economic and social stability which the Caribbean Basin Initiative poses.

WHEREAS: The Legislature of Puerto Rico understands that the treatment given Puerto Rico within the context of the Caribbean Basin Initiative is exceedingly unjust for the Island for the adverse effects which could be derived therefrom, places Puerto Rico at a historical crossroads, which requires that the Puerto Rican people set forth before the Congress, clearly and unequivocally, our people's indignation in the face of such unjust treatment.

NOW, THEREFORE: BE IT RESOLVED BY THE LEGISLATURE OF PUERTO RICO:

To express its feelings on President Reagan's Caribbean Initiative and petition the Congress of the United States that when considering the Caribbean Initiative, it heeds the claims of the People of Puerto Rico presented to the Congress through this Resolution.

1. . The Legislature of Puerto Rico, in solidarity with the aspirations of the Caribbean Nations to achieve economic, social, and political development within a democratic system, expresses its support of the President of the United States' objectives as set forth in his Caribbean Basin Initiative, of promoting the political stability of the Caribbean by means of economic development. The Legislature, likewise, supports the President's objective that Puerto Rico and the U.S. Virgin Islands also will "benefit and prosper" as a result of his program.

2. To offset the harmful effects of the Caribbean Basin Initiative, and so that the objective of "benefit and prosperity" may be attained, the Legislature hereby appears before the Congress to claim the measures, the rights and the powers specified hereinbelow:

CLAIM 1.- Grant Puerto Rico power to impose tariffs and other controls on imports of products from foreign countries.

CLAIM 2.- Recognize Puerto Rico's power to enter into bilateral and multilateral trade agreements with other countries as it has been recognized in the areas of culture, technology and sports.

CLAIM 3.- Grant Puerto Rico the power to control shipments of products to protect the local farm production for the time it needs to develop a competitive basis.

CLAIM 4.- Modify the Foraker Act and the Jones Act of 1920, to permit Puerto Rico to use foreign flag vessels in its trade with the United States.

CLAIM 5.- Federal Aid should be granted in the form of block grants which Puerto Rico, through its Executive and Legislative powers, can use for the reconstruction of its economy and for its development on a long-term basis.

CLAIM 6.- Assist Puerto Rico's tourist industry:

a) by eliminating the 24 hour limit on the time cruise-ship passengers may remain in the ports of San Juan, Ponce, Mayaguez, and any others that may be established in the future;

b. by permitting foreign cruise ships to transport passengers between San Juan, Ponce, Mayaguez, and other United States ports;

c. by eliminating import duties on goods purchased by tourists in Puerto Rico.

CLAIM 7.- Stimulate investment by Section 936 companies in Puerto Rico, by the:

a) Extension to them of the Accelerated Cost Recovery System and the Investment Tax Credits providing for the transfer of the benefits thereof to their mainland parents;

b) Authorization to include the costs of training, in the computation of net income under Section 936; and

c) prompt resolution of the questions concerning the valuation of research and development costs for the purpose of determining transfer prices to be used in the computation of net income under Section 936.

CLAIM 8.- Exclude rum from the one-way free trade arrangement proposed by the Caribbean Initiative.

CLAIM 9.- Exclude from the one-way free trade arrangement proposed in the Caribbean Initiative, those products which are important to the economy of Puerto Rico, such as, but not limited to electrical and electronics products, pineapple, and tuna before it becomes necessary to prove that serious injury has ocurred to Puerto Rican industry.

CLAIM 10.- Expand air routes served by American and foreign airlines between San Juan and foreign countries.

CLAIM 11.- Establish centers for vocational training, higher education, and business and professional training in Puerto Rico for the benefit of the Caribbean.

CLAIM 12.- Provide assistance for specific agricultural projects, such as, for example, growing sugar cane for the production of molasses for use by the Puerto Rican rum industry, and the development of alternate sources of energy.

CLAIM 13.- Establish separate quotas for Puerto Rico and the United States when setting beef-import quotas.

CLAIM 14.- Caribbean Basin countries shall not be given more favorable treatment in bilateral and multilateral agreements on imports of textile and apparel products made in the United States.

CLAIM 15.- Include Puerto Rico on a nondiscriminatory basis in federal programs, such as: (a) federal government procurement, (b) location and expansion of federal offices and installations.

3. This Resolution is the urgent effort of our Legislature to protect the interests of Puerto Rico and the claims of the rights and powers that belong to Puerto Rico within the framework of the problems aggravated by the Caribbean Initiative. The Legislature feels that this is only one stage in the discussion of the problem, and proposes to initiate a process of consulting the various political sectors of the Puerto Rican community, to reach a consensus on the procedures that will allow the People of Puerto Rico to express to the Congress and to the President of the United States, their will with regard to the political, economic and social relationship between the People of the United States and the People of Puerto Rico.

4. To designate a delegation composed by the President of each Chamber of the Legislature, to appear before the Congress and its Committees, present a copy of this Resolution translated into English, and to urge the approval of the claims set forth herein.
5. To send a copy of this Resolution translated into English to the President of the United States.

Yo, Julio M. García Passalacqua, Secretario
de la Cámara de Representantes de Puerto Rico

CERTIFICO

Que la presente es copia fiel y exacta
del texto aprobado en Votación Final de la

Capitolio

SECRETARIO

ECONOMIC REPORT AND
SUMMARY OF TESTIMONY

before the

SPECIAL JOINT COMMISSION OF
THE LEGISLATIVE ASSEMBLY OF
THE COMMONWEALTH OF PUERTO RICO

on the

EXPECTED IMPACT ON PUERTO RICO OF THE CARIBBEAN BASIN INITIATIVE

INTRODUCTION AND SUMMARY

The Legislative Assembly of the Commonwealth of Puerto Rico held hearings before a Special Joint Commission to determine the "expected impact of the Caribbean Basin Initiative on the economic, social, and political life of the people of Puerto Rico". Between March 12, 1982 and March 19, 1982, the Commission heard members of the Puerto Rican community discuss how President Reagan's proposed program for other Caribbean countries would affect particular aspects of life in Puerto Rico. The statements of many of these speakers also covered the adequacy and applicability of President Reagan's proposed measures for Puerto Rico.

There was a strong consensus among witnesses, both with respect to the impact -- it will be adverse -- and reasons why Puerto Rico will find it extremely difficult to offset or to recover from the adverse effects. The reasoning is summarized as follows:

- The economy of Puerto Rico is structurally weak.
- Current weakness is manifest in a persistently high rate of unemployment -- currently over twenty percent.
- Long-term problems are indicated by:
    - A very small proportion of the population participating in the labor force.
    - Low or negative rates of net investment in productive facilities relative to net product.

- The current federal fiscal policy is draining the resources which Puerto Rico needs to correct its structural economic problems.

- The agricultural sector of Puerto Rico is similar to that of Caribbean Basin countries and dissimilar to that of the United States:

  - Caribbean Basin country exports of tropical fruits and vegetables will compete directly with Puerto Rican products in mainland markets.

  - Numerous Caribbean food products will be exported primarily to Puerto Rico, not the mainland, thereby impeding Puerto Rico's attempts to reduce its dependence on food imports.

- The manufactured products Caribbean countries are best able to produce and export are highly labor-intensive. Production in these countries is likely to replace Puerto Rican production. The result will be reflected directly in higher rates of unemployment in Puerto Rico.

- Without an adequate domestic supply of molasses, Puerto Rican rum producers will be unable to compete for sales in mainland markets if the United States duty on rum is removed. The result will be the loss of an industry that is the source of pride and tradition in Puerto Rico.

- The measures for Puerto Rico proposed by President Reagan are inadequate to offset the anticipated injury to Puerto Rico or "to promote economic revitalization and facilitate expansion of economic opportunity" in Puerto Rico:

  - Rebate to Puerto Rico of excise taxes on imported rum is a form of federal handout that will not save jobs, promote economic development, or promote self-respect.

  - Federal "advice and assistance" on tropical agriculture and forestry research will not facilitate Puerto Rico's intensive efforts to produce its own food.

  - Extension of investment tax credits and accelerated cost recovery to firms in Puerto Rico may serve to keep capital-intensive businesses here, but is unlikely to absorb the large number of persons unemployed by the other proposals in the President's Caribbean Basin program.
  - Safeguard investigations of Puerto Rican industries after serious injury has been inflicted are meaningless. Once firms have left Puerto Rico and relocated elsewhere, they are unlikely to return.

- The combination of Puerto Rico's structural problems plus those problems created by federal fiscal policies renders the Puerto Rican economy incapable of absorbing the adverse impact of the Caribbean Basin Initiative program. As a consequence, unemployment will continue to increase, bringing with it frustration, anger, and social unrest, particularly when a whole generation of young people can find no productive activity. The alternative is wholesale migration to the States.

In the remainder of this report, the facts and opinions brought out in the testimony are summarized and put into the context of Puerto Rico's current economic situation. Particular emphasis is on testimony concerning the economic and social consequences of the Caribbean Basin Initiative.

I. STRUCTURAL ECONOMIC WEAKNESS

The economy of Puerto Rico is weak. At present, this weakness is seen most vividly in high and persistent unemployment. Witnesses at the hearings of the Special Joint Committee explained that the underlying structural problems are not short-term, but can be expected to continue, absent a concerted effort to redirect the Puerto Rican economy. In their view, the Caribbean Basin Initiative will limit Puerto Rico's ability to restructure and, at the same time, will impede any efforts to do so.

Unemployment Today

Puerto Rico's highly successful economic development plan of the 1950's brought the average level of unemployment down to 10 to 12 percent. Today, the official rate of unemployment is over 20 percent.

Having 20 percent of your labor force unemployed presents serious economic and social problems to any society at any time. The severity is accentuated in Puerto Rico because of the unusually low rate of participation in the labor force. Only 30 percent of the Puerto Rican population is working or actively seeking work. The ratio for the United States as a whole is closer to 50 percent.

This combination of high unemployment and low activity leads to the fact that fewer than one-quarter of the Puerto Rican population is employed. Thus, the loss of a job by one Puerto Rican leaves four people without support.

Economists are in general agreement that the underlying cause of unemployment in Puerto Rico is the change in the structure of the economy. The current economic recession only aggrevates an existing condition.

Structural problems are common to developing countries. As industrialization advances, the the traditional low skilled, highly labor-intensive activities decline and more capital-intensive activities requiring higher levels of education and training replace them. Since the newer activities require less labor, they must grow at a faster rate than traditional activities decline in order to prevent rising unemployment. This balance was fairly well maintained in Puerto Rico until the early 1970's. While the average level of unemployment was 10 to 12 percent, it was not increasing.

In the 1970's, the balance was upset. Costs of production rose unusually fast in Puerto Rico for energy and for labor. As a result, the loss of jobs in labor-intensive industries, such as apparel, accelerated and new industries could not absorb all of the displaced workers.

The magnitude of the imbalance was concealed for several years because the public sector hired increasing numbers of workers. Between 1970 and 1980, the government of Puerto Rico provided jobs for 140,000 workers. This was equivalent to over one-third of the additions to the Puerto Rican labor force during the 1970's. Many of these jobs were funded with federal aid, for example, CETA public service employment and employment administering federal programs such as food stamps.

The decline in federal funding now in process has added to unemployment today. A recent report showed that there was an 8.5 percent decline in public service employment between the end of 1980 and the end of 1981. With federal fiscal policy becoming more restrictive, it is anticipated that government jobs in Puerto Rico will not increase in the foreseeble future. As brought out by economist Elías R. Gutiérrez, federal fiscal policies hasten the deterioration of the Puerto Rican economy.

Long-Range Outlook

The effects of a severe reduction in federal funds and a prolonged period of high unemployment tend to be cummulative. When combined with the particularly high rate of unemployment among young people and the low level of private investment in productive facilities, the outlook for an early recovery is bleak.

In late 1981, nearly half of the young men in Puerto Rico and one-third of the young women who were seeking jobs could not find work. These young people, between 16 and 24 years of age, are starting their working lives with no work experience, no job discipline, and soon little or no respect for an economy and society that keeps them idle. With extended unemployment, their capabilities and willingness to contribute to Puerto Rico in the future will be diminished.

The other aspects of the Puerto Rican economy that will impede long-term progress are the negative rate of personal savings and declining rate of private investment. Professor Alfredo González Martínez, Professor of Economics at the University of Puerto Rico in Mayaguez, emphasized the importance of these deficiencies. With respect to personal savings, Professor Martínez explained that through years of prosperity, the incomes and standard of living of Puerto Rican people rose. Then, when work became scarcer and inflation eroded buying power, the habit of buying did not change. The use of credit rose to finance consumer products. The result has been a negative rate of personal savings and a drain on funds that might otherwise be used for investment in productive plant and equipment.

High rates of interest on short-term investments also have drawn funds from investment in fixed plant and equipment. In fact, Professor González Martínez explained, the ratio of fixed capital investment relative to net product has been falling. Old plant and equipment is not being replaced at the same rate it is wearing out. Thus, future economic recovery will be hindered by lack of productive capacity.

II. THE CARIBBEAN BASIN INITIATIVE: ADVERSE EFFECTS ON PUERTO RICO

Virtually every businessperson, economist, and government official who has examined the Caribbean Basin program has stated that it will have an adverse impact on the Puerto Rican economy. During the hearings before the Special Joint Commission, many statements were made and read. Among these were the following:

Letter from Mr. Richard Williamson, Assistant to the President for Intergovernmental Affairs, Office of the White House

Trade Policy Committee of the United States Special Trade Representative

Governor Romero-Barceló

Mayor Hernán Padilla

Senator Hernández Agosto

Puerto Rican Manufacturers' Association

Dr. Elías R. Gutiérrez

Association of Puerto Rican Producers

Puerto Rican Milk Producers' Association

International Brotherhood of Teamsters, Local 901

Puerto Rican Workers' Syndicate

Senator Francisco Aponte Pérez

Former Governor Roberto Sánchez Vilella

Former Governor Rafael Hernández Colón

Reverend David Pérez Colón

Former Secretary of State Guillermo Irizarry

Dr. Arturo Morales Carrión, former U. S. Assistant Secretary of State for Latin America Affairs; former President of the University of Puerto Rico

Antonio González Chapel, former Secretary of Agriculture.

Alfredo González Martínez, Professor of Economics of University of Puerto Rico at Mayaguez

Dr. Antonio González, former Dean of Social Science of University of Puerto Rico, economist and former President of Puerto Rico Union Party

Attorney Juan Manuel García Passalacqua, Member of the Constitutional Commission of the Puerto Rico Bar Association

Professor Luis Passalacqua Christian International Law Professor University of Puerto Rico

Dr. José Joaquín Villamil, Economist

José Olivari, former Secretary of Agriculture

Professor Adrián Díaz Ruiz, University of Puerto Rico, Economist

Francisco Pujols, Executive Director, American Express Puerto Rico

Carmen Gautier Mayoral, Professor of Government and Expert in International Relations

Pedro González, C. P. A.

Professor Angel Calderón Cruz, Director of Caribbean Studies Institute of University of Puerto Rico.

Attorney Juan Mari Bras, Secretary General of the Puerto Rico Socialist Party

Attorney Rubén Berríos Martínez, President of the Puerto Rico Independence Party

Mon. Héctor M. Rivera, Auxiliary Bishop of San Juan

League of Cooperatives

The component of the Caribbean Basin Initiative that is expected to injure Puerto Rico the most is the one-way Free Trade Arrangement. At their present stage of development, Caribbean Basin countries will concentrate production and exports on agriculture, processed foods and related products, and on manufactured products requiring substantial amounts of unskilled labor. Each of these areas is discussed below in a separate section.

The combination of structural weakness in Puerto Rico's economy plus federal fiscal policy will preclude economic responses that would allow Puerto Rico to absorb the anticipated adverse effects.

President Reagan has proposed measures to help Puerto Rico and the U.S. Virgin Islands. Most of the witnesses were forthright in denouncing these measures as inadequate to promote economic prosperity in Puerto Rico. In fact, the proposed measures would not even compensate Puerto Rico for injury done by the Caribbean Basin program, so that the Puerto Rican economy will regress rather than progress.

III. AGRICULTURE

Agriculture is the backbone of the economies of most of the Caribbean countries and accounts for the largest share of their exports. Having the same climate and growing conditions and often similar cultural backgrounds, these countries and Puerto Rico produce many of the same food products. Many of these products are not grown on the mainland United States.

Puerto Rico already has lost sales in the United States mainland markets. Under multilateral trade negotiations and the Generalized System of Preferences, Caribbean countries have been granted duty-free access to the United States for many products, but particularly those not grown on the mainland. The products protected from past trade concessions generally have been those important to farmers in the States -- sugar, beef, avocados, tobacco. Some concessions have been granted on competitive fruits and vegetables, but the lower duties are applicable only during offseason for mainland crops.

The United States now is seeking to give developing countries in the Caribbean more and larger trade concessions. Based on past experience, Puerto Rico will face a substantial increase in imported agricultural products. This will reduce Puerto Rico's shipments to the United States. But, even more important, since the duty cuts apply equally to products entering the Commonwealth, the impact will be particularly hard on Puerto Rican farmers selling in their local markets. In this situation, the attempt by the United States to help its neighbors can have a direct and severely adverse effect on the economy of Puerto Rico. This conclusion was explicit in the testimony of Puerto Rican agricultural experts.

Puerto Rican Agricultural Development

In the process of establishing a viable industrial sector, the structure of the Commonwealth's output has changed, with the share contributed by agriculture declining significantly. In 1950, agriculture comprised 11.5 percent of gross product. By the 1970's, agriculture's share had fallen to just over three percent.

During this 30-year span, Puerto Rico's population continued to grow, as did per capita income. A rising standard of living brought with it a demand for more and more varied food. Professor González Martínez also cited the widespread use of food stamps in Puerto Rico as a stimulous to food consumption.

At the present time, the value of domestic agricultural production is rising less than 15 percent per year while the value of food consumed is growing at an annual rate of over 20 percent. Under the most favorable conditions, this situation is unstable. Without adequate production of food to feed larger urban populations, Puerto Rico has been unable to sustain the spectacular economic growth that characteried its economy in the past.

Puerto Rico's lagging agricultural sector has necessitated the use of scarce capital to import food rather than raw materials and capital equipment. This hinders development by failing to support the growth of population and income in rural and urban sectors. First, widespread unemployment and lower incomes persist in the farm sector. Since income in the rural sector is low, the industrial sector has a much lower local demand for its products. Next, the need to import large quantities of food -- over 80 percent of domestic consumption -- expands the growing trade deficit, thus imposing a large and growing burden on the economy. And third, agriculture still employs 43,000 workers; alternative employment for these Puerto Ricans is unlikely to be found.

Exports to Puerto Rico

As Caribbean Basin countries increase their capacity to export under the impetus of one-way free trade, they are likely to concentrate on Puerto Rico. Agricultural experts in Puerto Rico have testified that many of the products that will be imported duty-free into the United States are foods that are consumed primarily by Puerto Ricans, whether in Puerto Rico or on the mainland. Among the products listed by Antonio González Chapel, former Secretary of Agriculture, were plantains, coffee, and various root vegetables.

In the case of products produced both in Puerto Rico and on the mainland and for which there is a Commonwealth market, trade concessions are likely to have their major impact on the

Commonwealth, not on the mainland. The principal reasons are: (a) the shorter distance to Puerto Rico makes the Commonwealth a more attractive market for these countries, and (b) the enormous difference in size between the mainland and Puerto Rico makes marketing and distribution less complex and less costly in Puerto Rico.

The effect on the agricultural development program in Puerto Rico could be disastrous since many of the products that will enter duty-free are those on which Puerto Rico is concentrating, in its current 12-year Plan for a Modern Agriculture. This Plan, started in 1977 to reduce Puerto Rico's dependence on imported food, includes a Truck-Farming Program. Among the fruits and vegetables covered by this program are tomatoes, peppers, eggplant, papaya, cantalope, and sweet potatoes. Most of these products have been protected from past trade concessions, but now would be subject to free trade. Puerto Rico will have a difficult, if not impossible, task in competing in its local markets.

The recommendation of numerous witnesses was that some means be used to protect Puerto Rico's local agricultural sector until it reaches efficient size. Amongthe alternatives suggested were the following:

- Grant Puerto Rico authority to control imports into Puerto Rican markets either by tariffs or other controls.
- Exempt agricultural products important to development in Puerto Rico from duty-free status.
- Exempt agricultural products important to development in Puerto Rico from duty-free status when exported to Puerto Rico.

Meat Import Quotas

A pointed example of the disproportionate impact on Puerto Rico of federal trade policies is the effect of the Meat Import Law of 1964. Under this law, United States imports of fresh, chilled, or frozen meat may be limited in any year when estimates of such imports exceed an amount determined by formula.

United States imports from Caribbean countries account for less than 15 percent of total U.S. imports, including those into Puerto Rico, but they comprise over 95 percent of foreign beef imported into the Commonwealth. One reason is that the quality of Central American beef products is the same as that of Puerto Rican, so they are directly competitive, whereas mainland beef is higher quality. Another reason is the relatively high prices for beef in Puerto Rico due to the high cost of imported feeds and the lower scale of operation. This may make sales in Puerto Rico more profitable. Beef imported into Puerto Rico often sells at a higher unit value than beef imported into the rest of the United States.

When the United States limits its beef imports from every country, the Central American countries are more likely to ship their quotas to Puerto Rico than the mainland. This occurred in 1975 when import restrictions were imposed. Exports from Caribbean countries to Puerto Rico rose 40.3 percent, while exports to the United States, excluding Puerto Rico, increased only 5.7 percent.

Each of the Central American countries has had restrictions on imports of foreign beef and dairy products and on the export of domestic cattle. High import duties, export licenses, exchange controls, and advanced deposits are some of the restrictions employed to aid their industries. Nicaragua, for example, has been a consistent exporter of beef to Puerto Rico. All beef trade in Nicaragua, internal and external, has been controlled by a central agency. Beef has been imported only when domestic production is inadequate to meet demand. The export of cattle also has been regulated by this agency.

Puerto Rico has virtually no control over beef imports. The Commonwealth is unable to protect its own beef market from foreign imports in order to give its industry an opportunity to grow and become more productive.

By directing a large proportion of Central American beef exports to Puerto Rico, the U.S. meat quota regulations adversely affect Puerto Rican production. To alleviate the problem, United States meat quotas should be calculated separately for Puerto Rico and for the mainland. This would allow Puerto Rico to control beef imports at a rate consonant with the need to supplement local production.

Poultry and Eggs

For some agricultural products, competition in Puerto Rico is primarily from mainland producers rather than from other Caribbean countries. Important examples brought out in the hearings were poultry and eggs.

Puerto Rico's consumption of poultry doubled during the 1970's. Through private and government efforts, local production was increased even more, 135 percent between 1979 and 1980. However, Puerto Rico still produces only one-third of its poultry needs. The rest is imported from the U. S. mainland.

The poultry industry is well-suited to Puerto Rico since it has high productivity per unit of land and can be operated by family groups. To be cost-competitive, according to Antonio González Chapel, a critical efficient size must be reached. Puerto Rico is striving to combine family groups under centralized management to achieve this size. In addition, local production of feed has been started in order to lower costs.

Further success in the island's poultry and egg development program requires time for farms to expand and reach efficient size. Antonio González Chapel contends that this will not occur as long as cheap poultry and eggs are shipped from mainland processors that have already reached efficient size. Puerto Rico needs authority to limit shipments from the mainland in order to give its industry an opportunity to reach a productive, competitive level. Antonio González Chapel has said that if Puerto Rico could produce the poultry and eggs it consumes, that 6,000 new jobs would be created directly.

If there is fear that the agricultural sector of the island will burden consumers with high food prices, it should be recognized that laws to control imports are largely a legislative matter, that Puerto Rico is as democratic as any place in the world, and that local consumers comprise a vocal and most effective political group.

IV. PROCESSED FOOD AND BEVERAGES

A logical first step in economic industrialization is the processing of agricultural products. Examples are canned fruits and vegetables, meat and fish products, beverages, and bakery and confectionary products.

Over 23,000 workers are employed in Puerto Rico in food and beverage processing operations. Certainly many of these jobs will be lost as Caribbean sales in mainland United States markets replace Puerto Rican sales. Two products of particular concern to Puerto Rico are rum and tunafish.

Rum

Puerto Rico is the largest producer of rum in the world. Over 95 percent of production is consumed in the United States. Puerto Rico's sale of rum in the United States has an economic importance to the Puerto Rican economy beyond direct employment and income. The excise taxes collected on sales of Puerto Rican rum in the United States contribute 10 percent of the total receipts of the Commonwealth government. This source of revenue has grown fairly steadily, despite the fact that there is no adjustment for inflation, that is, the tax is not levied as a percent of the price. A reduction in this income could severely damage the Puerto Rican economy, coming at a time when government receipts already are declining due to federal cutbacks and recessionary pressures. Thus, any adverse impact on the rum industry reverberates throughout the whole economy.

Of all concessions proposed in the Caribbean Basin Initiative, that on rum has the greatest potential for economic injury to Puerto Rico. The import duty on rum offsets externally imposed costs that cause Puerto Rican rum to be more costly. One such cost is that required to meet environmental regulations in Puerto Rico. A second, and more significant cost, is the freight paid on importing molasses, the main ingredient of rum.

Over 80 percent of the molasses used by the Puerto Rican rum industry is imported. The largest source is the Dominican Republic. Other suppliers are in Honduras, Jamaica, Barbados, and Trinidad, i.e., all countries that produce sugar cane. The cost of transporting molasses from these Caribbean countries adds 10 to 30 percent to the cost of a gallon of molasses, depending on the current price per gallon.

Puerto Rico is as concerned about the reliability of its supply of imported molasses as it is about the cost. The major suppliers of molasses Dominican Republic and Jamaica, also export rum to the United States in competition with Puerto Rico. With duty-free access to United States rum markets, these competitors, as well as other producers of sugar cane, are likely to reserve their molasses production for their own use in producing rum. President Reagan's suggestion that the administration encourage molasses suppliers to continue selling to Puerto Rico is not a guarantee that these suppliers will agree, or for how long they might agree.

If the rum industry is to be viable in the future, Puerto Rico must continue efforts to expand its supply of domestic molasses. One possibility is that rather than provide Puerto Rico with non-specific assistance for research and development in tropical agriculture, as proposed by President Reagan, that federal aid could be directed to an immediate and specific problem -- development of sugar cane for the primary purpose of producing molasses for the Puerto Rican rum industry.

Foreign rum imports already have begun to increase, spurred by the United States duty cuts in the 1979 Multilateral Trade Negotiations. If the United States now were to grant duty-free access to its rum markets, distributors of rum imported from beneficiary Caribbean Basin countries would have another $3.00 per case to use to promote their brands in United States markets. Since their costs are already below Puerto Rico's, the $3.00 could be used for advertising and/or to increase wholesalers' margins.

Distributors are looking for higher volume and margins. If they can achieve both by buying imported rum, they are likely to do so. Sales of Puerto Rican rum will be replaced by imported rum from Puerto Rico's Caribbean neighbors.

Under these conditions, rum distilleries in Puerto Rico will be forced to curtail operations; production is economical only when the product can be sold.

As compensation, President Reagan has proposed that the U. S. excise tax collected on imported rum be shared by Puerto Rico and the U. S. Virgin Islands. One witness, Dr. Antonio González, termed the proposal "infantile". In his view, this would be another federal handout. Instead of increasing its economic self-sufficiency, Puerto Rico would become more dependent on the federal government.

Moreover, the Puerto Rican rum industry has a long history in Puerto Rico. It was a major factor in the Commonwealth's economic development in the 1950's and 1960's. To destroy that industry, now, when the economy is in a turmoil, would be just one more blow to Puerto Rican self-pride. The rationale for such a sacrifice is not at all obvious. Puerto Ricans are unanimous in their request that the United States import duty on rum not be eliminated at this time.

Tuna

In 1980, Puerto Rico shipped over $365 million of canned fish to the mainland United States. Almost all of this was tuna. Canned tuna, by value, is the single largest Puerto Rican export to the United States. Shipments have been growing 10 to 15 percent per year.

The tuna industry employs over 7,000 workers in Puerto Rico. Operations are concentrated in the southern and southwestern parts of the island where unemployment is, otherwise, especially severe. The industry has been the dominent employer in Mayaguez and Ponce.

The current growth of the tuna industry is limited by the quotas on the number of porpoises that can be killed each year while catching yellow fin tuna. To avoid quotas and the higher U.S. minimum wages, cannery operators could relocate in countries in Central America, such as Costa Rica or Honduras, and still have duty-free access to U.S. markets under the Caribbian Basin Initiative.

V. MANUFACTURED PRODUCTS

Wage rates in Puerto Rico are at least three times higher than in most Caribbean Basin countries and generous benefit packages add to labor costs. These differences have already caused highly labor-intensive industries to move some of their production from Puerto Rico to neighboring islands and to Central America.

Granting trade concessions to Caribbean Basin countries on labor-intensive products can only accelerate the loss of jobs in Puerto Rico. Since the Puerto Rican economy, today, is unable to absorb workers at the current rate of displacement, new trade concessions would represent a direct transfer of unemployment from the Caribbean Basin countries to Puerto Rico.

In order to prevent this intolerable burden on the Puerto Rican economy, witnesses recommended that the granting of trade concessions on highly labor-intensive product lines be reconsidered. The products are apparel and selected electrical and electronic products. While many other products could be included in this category, (e.g., footwear, textile mill products, and various rubber and plastic products), apparel and electronic products employ substantially more people in Puerto Rico. The apparel industry, alone, employs approximately 33,000 workers, over 20 percent of nonagricultural employment in Puerto Rico.

The importance of these jobs is not only in their numbers, but also in the type of worker employed. For example, nearly 85 percent of apparel workers are women. Their profile would have these characteristics: low skills, minimal education or training, partial or total support of family, no geographic mobility.

When these workers lose their jobs in the apparel and assembly-type industries, alternative employment is scarce and usually nonexistent. They become part of the hard-core unemployed and their families become public dependents.

U.S. Imports from Caribbean Countries

Caribbean export sales of labor-intensive products have grown rapidly within the present system of U.S. tariffs and quotas. The primary reason is that the very large labor cost advantages enjoyed by Caribbean countries is sufficient to offset U.S. import duties. A second reason is that many products are already subject to trade concessions by the United States.

1. Tariff Item 807.00 for Japan

Under Items 806.30 and 807.00 of the Tariff Schedule of the United States, U.S. import duties are imposed only on the value added in foreign countries when the product is assembled abroad using components produced in the United States. This allows U.S. firms to make the more capital-intensive components in the United States and then do the highly labor-intensive assembly work in a low wage country. For example, men's shirts may be completely cut in Puerto Rico, shipped to the Dominican Republic for final assembly, and then shipped to the United States mainland for sale. The duty is paid only on the low cost assembly operation in the Dominican Republic.

In 1980, textile products valued over $515 million were imported into the United States under Tariff Item 807.00. Duties were paid on approximately one-third of this amount.

The value of electrical and electronic products was far higher. Examples of 1980 U.S. imports under Items 806.30 and 807.00 are shown below. Each of the products is manufactured in Puerto Rico, also.

U.S. IMPORTS (1980) UNDER TARIFF ITEMS 806.30 AND 807.00
(millions of dollars)

Office Machines and Parts	$610.0
Resistors and Capacitors	176.4
Conductors	151.6
Electronic Memories	34.5
Equipment for Making and Breaking Circuits	179.9

The import values are totals for all countries, including those in the Caribbean Basin. For the latter, almost one hundred percent of their exports of these electrical and electronic products enter the United States under Tariff Items 806.30 and 807.00. The small proportion that does not, enters duty-free under the

Generalized System of Preferences. This program (GSP) grants duty-free access to U.S. markets for selected products from eligible developing countries.

The United States now proposes to eliminate all duties on imports of electrical and electronic goods from Caribbean Basin countries. The effect on these countries could very well be minimal. The major beneficiaries will be firms in Japan and Europe. They will be allowed to produce 75 percent of these products in their domestic factories, ship the components to the Caribbean for final assemply, and sell the finished product in the United States free of all U.S. import duties. For electrical and electronic products, the Caribbean Free Trade Arrangement is tantamount to unilateral trade concessions to Japan and Europe.

Disadvantaged will be competing firms in the United States and Puerto Rico. The existing Tariff Items 806.30 and 807.00 require that 65 percent of value be produced in the United States. Under the Caribbean proposal, no part of the value of the product need be American. The proposal in the Caribbean Basin Initiative to include the value added in Puerto Rico as part of the 25 percent value added in the Caribbean is not expected to be of any consequence to Puerto Rico, according to Dr. Elías R. Gutiérrez.

To prevent injury to competing firms in Puerto Rico, selected electrical and electronic products must be exempted from duty cuts. This was stated forcefully by the Puerto Rican Manufacturers' Association:

> "Any foreseeable damage should be prevented. Waiting for it to take place before searching for a remedy, which could be too late, is unacceptable."

The particular products to be exempted from one-way free trade will be determined by consultation between appropriate Puerto Rican and administration officials.

2. Apparel Quotas

President Reagan has exempted textiles and apparel from the proposed Free Trade Arrangement. United States imports of these products already are subject to import quotas.

Under the provisions of the International Multifiber Arrangement, the United States may impose import quotas on specific items of apparel on a country-by-country basis. Shipments for each country are monitored and, as they begin to "disrupt" the United States market, bilateral consultations are held and then a quota or quotas are set. At present, the United States has agreements with three Caribbean Basin countries: Costa Rica, Dominican Republic, and Haiti. The levels of their respective quotas reflect the levels of actual imports during the year before which consultations began,1980 for Costa Rica and mid-1979 for the Dominican Republic and Haiti. Thus, imports already are at a "market disruption" level when quotas are imposed; and the quotas maintain imports at that level, not at a reduced level.

The most important category of apparel manufacture in Puerto Rico is "Body-Supporting Garments". This segment of the industry is especially mobile: machinery is light and relatively inexpensive, manufacturing processes are automatic; and the product is a low value, high volume item, so that workers can be trained fairly easily. Imposing quotas on imports from one country shifts growth in demand to a neighboring country.

In 1980, the United States imported body-supporting garments from 12 Caribbean countries. Until 1978, all of the imports from Caribbean Basin countries entered the United States under Tariff Item 807.00, i.e., the garments were assembled, only, in the Caribbean. In 1978, Jamaica began exporting garments with greater value added. Jamaica was joined by the Dominican Republic and Nicaragua in 1980. One explanation is that with the escalation in Puerto Rican wage rates starting in 1978, lower labor costs elsewhere could offset the U.S. import duty. More firms were willing to do more than just assemble garments in Caribbean countries.

The implications are clear: (a) The U.S. import duty on apparel is insufficient to prevent a shift of the apparel industry from the United States to lower wage countries. (b) Quotas only slow down the exodus. (c) The area with the greatest gain is the Caribbean Basin.

The federal government's proposal to provide more liberal quota arrangements for apparel imported from

Caribbean Basin countries will act to accelerate the demise of Puerto Rico's apparel industry. The result will be a rapid loss of employment of low skilled workers in Puerto Rico and an intolerable burden imposed on the government of Puerto Rico to provide for these newly unemployed workers and their families. Therefore, quotas on imports from Caribbean countries should not be made more favorable than quotas on imports from other countries.

Shift to Less Labor-Intensive Industries

An essential element in Puerto Rico's program to move its economy from stagnation to growth is a restructuring of its manufacturing sector. Recognizing that its former advantage in low skill, low cost labor has gone, Puerto Rico is concentrating on attracting less labor-intensive industries. Among the products and industries Puerto Rico has been attracting over the past ten years are pharmaceuticals, professional and scientific instruments, non-electrical machinery, and the more capital-intensive and intricate electrical and electronic products.

Requirements of these industries go beyond low cost labor. They frequently are able to take advantage of the higher levels of education and training that are available in Puerto Rico and, moreover, often provide additional training in skills in short supply, including management skills.

These industries also require a more extensive infrastructure -- communications network; reliable and adequate supply of electric power; low cost modern transportation, both in Puerto Rico and between Puerto Rico and the mainland United States; and adequate commercial and financial services. Provision of an infrastructure is vital and useful to renewed economic progress in Puerto Rico. It is expensive, however. Under the present-day fiscal austerity, few resources are available for these necessary components of economic development.

As part of the program to assure that Puerto Rico will benefit and prosper from the Caribbean Basin Initiative, several measures must be taken to help Puerto Rico attract new industry: (1) Tax incentives to invest in Puerto Rico should be expanded to include investment tax credits and accelerated depreciation, as proposed by President Reagan. (2) The Jones Act of 1920 should be modified to allow Puerto Rico to ship to and from the mainland using lower cost foreign flag ships. (3) Puerto Rico's authority to enter into multilateral and bilateral commercial agreements, such as the Venezuela and Mexico petroleum purchasing facility, should be recognized. (4) Centers for vocational training, for higher education, and for business and professional training should be established in Puerto Rico for use by all Caribbean countries.

Puerto Rico should share proportionately in federal programs. Especially important are federal procurement programs and facility location programs. In addition, as an alternative to requesting economic assistance for specific individual development programs, Puerto Rico would prefer the annual block grant for economic development that currently is being discussed. Dr. Elías R. Gutiérrez introduced an economic model demonstrating the substantial economic growth that could be achieved within five years by careful application of the funds in such a development program.

VI. TOURISM

Tourism is a highly labor-intensive activity with potential for continued growth in Puerto Rico. The realization of this potential is a function of economic conditions and weather in North and South America and Europe and depends also on Puerto Rico's efforts to remain competitive with other Caribbean tourist and convention sites.

Worldwide economic and weather conditions cannot be controlled or predicted by Puerto Rico. A variety of measures can be instituted to make tourism in Puerto Rico more comfortable and more competitive.

One set of competitive actions are designed to enhance the physical attractiveness of the island for visitors. An analysis of measures already in progress as well as those that could be undertaken is contained in the recent United States Department of Commerce Interagency Study. Covered are international transportation; hotel accomodations, service, and cost; and air, water, and urban pollution. With the continued help of the goverment of Puerto Rico, improvements can be effected in these areas.

A second set of measures to bolster the competitive status of tourism in Puerto Rico are those requiring action by the federal government since they involve trade and transportation to and from the island.

Specific actions that have been recommended are these:

(1) Eliminate the 24-hour limitation on the time cruise ship passengers may remain in Puerto Rican ports;

(2) Permit cruise ship passengers on foreign flag ships to travel between Puerto Rico and other U. S. ports;

(3) Eliminate import duties on goods purchased by visitors to Puerto Rico; and

(4) Eliminate United States Department of Agriculture inspection of the baggage of passengers traveling from Puerto Rico to the mainland United States.

Each of these actions is designed to attract more visitors to the island and to encourage longer stays. A byproduct of these actions would be an increase in employment in retail and wholesale trade, as well as in directly affected tourist industries.

[From the San Juan Star, Mar. 21, 1982]

PUERTO RICO'S LEGISLATURE EXPECTED TO DENUNCIATE CARIB PLAN

(By HAROLD J. LIDIN)

The House was expected to approve late Saturday a resolution denouncing President Reagan's Caribbean Basin Initiative as a threat to Puerto Rico and demanding that Congress grant the island increased economic powers—including the authority to limit farm imports from the mainland.

The Senate did not vote Saturday, but is expected to approve the measure today.

The resolution also states that the demands for greater economic powers for the island is only the first phase of a proposed broad revision of the political, economic and social relations "between the people of the United States and the people of Puerto Rico."

The "concurrent" resolution does not require the approval of the governor. Speaker Severo Colberg and Acting Senate President Sergio Peña Clos will testify on the document when they appear Wednesday before the House Ways and Means Committee in Washington. A copy of the resolution will also be sent to the White House.

Peña Clos issued a statement earlier Saturday inviting Gov. Romero to join him and Colberg, in creating a "national consensus" to defend Puerto Rico from the alleged threat of Reagan's Caribbean program.

Romero, after battling the CBI in its formative stages, has gone on record as endorsing the proposal. He contends that Reagan, responding to La Fortaleza complaints, introduced a number of special features to shield Puerto Rico from the potentially harmful effects of the CBI.

The legislative resolution noted that "more than 25 measures" were proposed by representatives of the executive and legislative branches of the Puerto Rican government to soften the impact of the CBI. But the Reagan administration "rejected all of them" except for the proposal permitting U.S. subsidiaries here to "pass-through" certain tax benefits to the parent firms on the mainland, the resolution stated.

The "more than 25 measures" mentioned in the resolution was an apparent reference to recommendations made by Romero, Mayor Hernan Padilla and Senate President Miguel A. Hernandez Agosto. The last-mentioned, who underwent emergency heart surgery recently, is now convalescing.

The demands made in the concurrent resolution, almost in their entirety, echo recommendations made by many of the 40 witnesses who appeared at the week-long, joint public hearings held by special committees of the House and Senate.

The major surprise in the list of demands was the petition that Puerto Rico be given power to limit the import of farm products from the U.S. mainland. Only one witness, former Secretary of Agriculture Antonio Gonzalez Chapel, had urged the proposal.

The document, as initially drafted, called for the federal government to give Puerto Rico the authority to "to control shipments from the United States to protect local production." This sweeping request was trimmed, in a Popular Democratic Party caucus, to cover farm products. Specific mention is made in the caucus-approved version to the power to curb imports of chicken, pork and eggs.

Notably missing from the list of requested powers is the authority for Puerto Rico to limit immigration. Severo Colberg, Jr., son of the House Speaker and one of two executive secretaries for the House Special Committee, said the caucus decided against including this demand because the immigration issue is highly political and the legislators wanted for now to focus directly on economic issues.

The resolution lists 15 demands upon Congress to grant new powers to Puerto Rico, to recognize powers which the local Legislature claims Puerto Rico already possesses.

The "new" powers the Legislature demands include:

Authority to limit farm imports from the United States.

Authority to impose tariffs or other controls on imported foreign products.

The powers which Puerto Rico allegedly holds under the existing Commonwealth status, and which the Legislature wants the Congress to recognize explicitly, include:

Authority to make commercial treaties on a bilateral or multilateral basis. Numerous witnesses urged that Puerto Rico seek membership in the San Jose Pact, an agreement by which Venezuela and Mexico supply nine Caribbean nations with crude oil on liberal credit terms. PDP president Rafael Hernandez Colon, testifying before the committee, said Puerto Rico could economize 25 percent on its oil expenditures if it were a signatory to the San Jose Pact.

Other action requested of the federal government includes:

Exemption of Puerto Rico from the cabotage laws to permit Puerto Rico to use foreign flag ships in its trade with the United States.

Providing federal aid to Puerto Rico in the form of block grants, so that Puerto Rico can use the money "for the reconstruction of its economy—

Permitting foreign flag cruise ships to remain in Puerto Rican ports for more than 24 hours.

Eliminating import duties on products acquired by tourists in Puerto Rico.

Eliminating inspection by the U.S. Department of Agriculture of passenger luggage on flights from Puerto Rico to the United States.

Stimulating investment here by 936 companies by extending to them the "Accelerated Cost Recovery System" and "Investment Tax Credits" on a pass-through basis, so that the benefits can be transferred to the mainland parent firms. This has already been proposed by the president.

Prompt resolution of the controversy over determination of proper costs for research and development to determine patent transfer rights for 936 companies.

Exclusion of electronic products, pineapple and tuna fish, among others, from the list of items to be allowed in tariff-free from the Caribbean countries without local industry having to prove it will be seriously hurt.

Elimination of rum from the free trade agreements contemplated under the CBI.

Expansion of airline service, both foreign and U.S., between San Juan and foreign countries.

Mr. **Colberg**. Now, Mr. Chairman, the Acting President of the Senate, Hon. Sergio Peña Clos.

Mr. **Peña Clos**. Mr. Chairman and distinguished members of the committee, the statement which the Speaker of the House of Representatives has read to you on behalf of the Puerto Rican Legislative Assembly is the result of the first and only public discussion in Puerto Rico on the subject of the Caribbean Basin Initiative. Most importantly, it is the first activity in which the people of Puerto Rico, representing different political, economic, and social oraganizations were able to express their positions concerning the expected impact of the Carribbean Basin Initiative.

We are exercising a mandate entrusted to us by the people and the constitution of Puerto Rico. We have set aside our own personal aims with regard to the political status of Puerto Rico because we believe that at this time, the priority must be the economic survival and economic development of the more than 3 million American citizens who live in Puerto Rico.

If we are not heard, we fear what will happen to our economy and, more importantly, to our people. If you destabilize Puerto Rico, you will destabilize the rest of the Caribbean, and the objectives of the Initiative will have been defeated.

We are sorry that officers of the Commonwealth—in misuse and disregard of the democratic process—have tried to challenge and undermine our effort to present to you the expected impact on Puerto Rico of the initiative. We hope that you, on the other hand, will give close and detailed consideration to the documents we have presented today; for they evidence the effort and the consensus of many Puerto Ricans, distinguished in Government, in business, in agriculture, education, and religion in our society. They represent more than a million fellow citizens who think and agree that the initiative harms and imperils Puerto Rico's economic development.

Thank you, Mr. Chairman and members of the committee. The Speaker and I, as well as members of our staff, are ready and willing to answer your questions.

Chairman **Gibbons**. Thank you, Mr. Senate President.

I want to go to page 1 of the Speaker's statement and ask some questions about the articles that are at the top of the page, if I may.

What is meant by "assure that selected products which are vital to Puerto Rico's economy are exempted from trade concessions before Puerto Rican industry is injured"? What products do you have in mind and how would you like to have these exempted?

Mr. COLBERG. Especially, Mr. Chairman, our processed agricultural products. For the benefit of giving precise answers to you, I will ask our adviser, Dr. Barbara Epstein, to give you all of the details on the questions.

Dr. EPSTEIN. The most important product in this category would be rum. It is sort of the backbone and the pride of Puerto Rico to have produced this rum industry. Its biggest problem right now is lack of an adequate source of domestic molasses. They are trying to correct this and they need more time to do so. They are not asking that the duties stay on forever, but that you wait before reducing it to zero and give them time to do this.

The other products of particular concern are some of the electrical and electronic products that are made in Puerto Rico because of a lower labor cost. The big concern here is that the competition will come from, not directly from the Caribbean countries, but from European and Japanese countries who will now have access to the U.S. market at duty-free rates.

I would say the other product is probably tunafish.

Chairman GIBBONS. What is meant by "free our tourist industry from noncompetitive restrictions, for example, the 24-hour limitation on cruise ships visiting Puerto Rico"? I am not familiar with that issue.

Dr. EPSTEIN. There are several regulations that put the Puerto Rican tourist industry at a disadvantage compared to other Caribbean countries. One is that the tourist ships that come into Puerto Rico are allowed to stay in port only 24 hours and then they must move on.

Chairman GIBBONS. Why is that? What was that regulation ever imposed for?

Dr. EPSTEIN. We are still looking for a good answer, but it is in the law and we think it is in the Jones Act, but I would have to go back and check that.

Chairman GIBBONS. That is an old restriction or a new restriction?

Dr. EPSTEIN. Yes, it was an old one.

There are other restrictions such as free-port type of operations. Puerto Rico does not have ability to suspend duties for goods that tourists purchase in Puerto Rico, so instead they go to other islands to do all of their shopping. This reduces business and retail and wholesale operations in Puerto Rico, and also the time that people stay there.

Chairman GIBBONS. That is because you are within the customs jurisdiction of the United States?

Dr. EPSTEIN. That is correct.

Chairman GIBBONS. So is the Virgin Islands?

Dr. EPSTEIN. That is exactly right.

Chairman **Gibbons**. On the "reduce the cost of shipping", I guess you are referring to the Jones Act there? Is that what you are referring to?

Dr. **Epstein**. Yes, very definitely. You can reduce it either by modifying the requirements of the Jones Act or by providing Puerto Rican shipowners and operators with the same type of assistance and subsidies that shipowners in the States receive. They do not get the benefit of those programs.

Chairman **Gibbons**. I didn't know that. You have the Jones Act one way, and you don't get the other benefits the other way?

Dr. **Epstein**. That is correct.

Chairman **Gibbons**. Why did we do that to you?

Dr. **Epstein**. That I can't answer.

Chairman **Gibbons**. It was done a long time ago?

Dr. **Epstein**. Yes.

Chairman **Gibbons**. Unfortunately this committee doesn't have control of the Jones Act. Perhaps we can get some cooperation from the Merchant Marine Committee, and that is something that the staff ought to make a note of.

Now you have two other things about controlling imports into its market. That is the first item.

What are you talking about there?

Dr. **Epstein**. The concern here is for the agricultural sector of Puerto Rico.

Chairman **Gibbons**. Are you talking about imports from other islands, is that right?

Dr. **Epstein**. Yes.

Chairman **Gibbons**. Or from the CBI countries?

Dr. **Epstein**. Primarily the CBI countries because they are the ones that have been shipping products into Puerto Rico. In many cases, these are food products that don't necessarily come to the States at all. Their food consumption habits are very similar to those in Puerto Rico and the kinds of products that they use. What it does is open up Puerto Rico's market directly for agricultural competition from the Caribbean.

Chairman **Gibbons**. What kind of competition would you expect in that area?

Dr. **Epstein**. Well, we have already seen some of it. Puerto Rico is trying very hard to develop what is called a truck farming program. It imports 85 percent of its food requirements now.

Chairman **Gibbons**. I am sorry I missed that.

Dr. **Epstein**. Puerto Rico is now importing about 85 percent of its food requirements and it is trying to stop that, so that it can use the money for other purposes. It is trying to develop a fruits and vegetables industry and its beverage industry.

I will give you an example of what happened when they attempted to increase peppers and tomatoes. It came to Lent season last year and they were ready to pick these vegetables for the increased demand at that time. The Dominican Republic sent in about five full vans of these same exact vegetables at prices which caused the Puerto Rican farmers to say "It will not pay us to pick the vegetables off the vines; we cannot even cover the cost of picking them." So they just let them sit there on the vines and they were dumped.

Chairman GIBBONS. What you would like to have in this Caribbean Basin is an agreement or legislation or something that said to the effect that the Puerto Rican legislature or its government could set some kind of import duty on competitive agricultural products coming in just for use in the Puerto Rican market?

Dr. EPSTEIN. That is right, or other types of control that will allow Puerto Rico to control the volume of products coming in, and to relate that volume to their own program for increasing production within Puerto Rico.

Chairman GIBBONS. I am not sure what you want to do on these international agreements. Could you explain that to me further? You want power to enter into international agreements such as the San Jose Agreement?

Mr. MILLMAN. If I might respond, the San Jose Agreement is an agreement between Venezuela and Mexico and other Caribbean nations. Pursuant to the agreement petroleum is made available at substantially reduced costs, about 30 percent below the world market.

There is no reason whatsoever, given the status of Puerto Rico, that Puerto Rico cannot enter into that agreement and purchase oil at below the world market. In fact there have been expressions of interest by Venezuela. The President of Venezuela has indicated that he would invite this and there is substantial authority which we can cite including articles which recognize Puerto Rico's ability to enter into international agreements such as this. Additionally, Puerto Rico might want to enter into commercial agreements with the other Caribbean nations with whom it is competing, or certainly will be competing with more directly if CBI is enacted.

It would turn Puerto Rico outward toward the Caribbean and make it competitive with nations whose economies and structures are more similar in size to that of Puerto Rico.

I would like to go back one moment, Mr. Chairman, to your preceding question about imports. There is precedent in the Tariff Act of 1930 to allow Puerto Rico to control or impose duties on coffee. It is in place to protect the Puerto Rican coffee industry. It was enacted in the 1930 legislation because the Puerto Rican coffee industry had been damaged in a hurricane.

So what we are saying to you here today does not suggest any new approach or any new added status in terms of the capacity of Puerto Rico to do certain things. It has the capacity subject to congressional authorization.

Chairman GIBBONS. Essentially then in your first four items you are saying you want to control what goes on within the confines of Puerto Rico and only the confines of Puerto Rico, is that right, except reducing the cost of shipping?

Mr. MILLMAN. With that observation, that would be correct, Mr. Chairman.

Chairman GIBBONS. But the fifth one would really include the shipping of products into this mainland market, is that right?

Mr. MILLMAN. That is correct. You are talking about point No. 5?

Chairman GIBBONS. Yes, point No. 5.

Mr. BAILEY. Mr. Speaker and Mr. President, I invite your comments, but first I want to welcome you. We are happy to see you here, and we are very happy to have an opportunity to talk with you.

I have been listening to the testimony this morning, and I have some very serious reservations about the Caribbean Initiative myself, so I can share some of those feelings.

Just to follow up on something that the chairman asked, my concern, though, is, what is your party's point of view on the relation of Puerto Rico to the United States? The reason I want to ask that is in connection with the view, Mr. Speaker, in your statement on the tariff thing and comments that you just made about the coffee.

Mr. **Colberg**. The popular Democratic Party is an advocate of commonwealth status and free association with the United States and we have been asking for many years to improve the status along some of these lines and other different things.

We have been unsuccessful here in Congress. They claim we are asking too much. But right now, more than we have asked in past years, has been recognized by the present administration in the case of the Marshall Islands and the other islands. So there are the precedents on what we ask for.

Mr. **Bailey**. Incidentally, I don't pretend to be an expert on the history of the status issue and I don't want to go into that. Your Delegate here in Congress yesterday requested we not get into that issue, and I just want to raise some questions about it. I respect his views and I respect your views, and I understand they probably would be different in terms of that status.

Just as a personal view on my part, I am very proud that Puerto Ricans are American citizens and that we are American citizens together. I am very proud of that. I really am.

My fear is that with some of the tariff ideas here or the authority issue on the tariff, doesn't that tend to take you more away from us? Maybe my prejudice is showing that I want to be closer to you, but wouldn't it have that effect? Is that wise, and I wonder about the issue in 1930. That is a technical precedent and I understand that.

Mr. **Peña Clos**. I think it would bring us closer to the United States.

Mr. **Bailey**. How would it do that?

Mr. **Peña Clos**. It would bring us closer because we would be receiving top consideration due to our condition of American citizenship and we would like to stress right now that with regard to the political status of Puerto Rico, it is not our priority. The economic effects of the CBI are involved there.

Mr. **Bailey**. I apologize. I don't want to touch a nerve here and please forgive me if I do. I just want to express the opinion that the well-being of Puerto Rico is as important to me as the well-being of any American citizen.

To me, as a Representative elected from Pennsylvania, I want you to know it just bothered me, that portion of the statement that you made. I understand your concerns and I respect them and I know you care very much about people, I am sure everywhere in the United States, and to me that includes Puerto Rico.

I think I was a little concerned that the effect of that kind of policy, what it would be in terms of the authority issue and I think you understand what I mean.

Mr. **Ramírez**. You have two items, a second item in the resolution. One is related to import duties or tariffs, and the next one is related to the authority to make international agreements.

Now, what we claim in relation to the second one, that problem has been decided and Puerto Rico has the authority to carry on these agreements. There are two important legal papers, one by a professor at Yale and the other is by a lawyer well known in the States, that claim that Puerto Rico already has that power.

The resolution was only asking for the recognition of that power by Congress, because what has happened in the history of this clause is that at one moment when Puerto Rico was invited to participate in the Caribbean Bank, the attitude of the Government of the United States was in favor of it and so they recognized the right. But when the administration is not in favor of the particular agreement, they reject it.

So what we would like to have is a clarification and a recognition of whether we have the right or not. In relation to this which has been asked by the Puerto Rican people in the past, the difference is this: At this particular moment of the Caribbean Basin Initiative, you are giving the Caribbean countries something that Puerto Rico had for a long time, that is free trade. But in relation to many articles, you are not really giving free trade into the United States. You are giving free trade into Puerto Rico.

The Puerto Ricans are the only ones who buy those products. What we are asking for is the right for the Puerto Ricans, the ones affected by this, to, in a way, participate in defending the Puerto Rican economy.

So I don't believe that this clause would ever take us away from the United States. On the other hand, it would be within the system and I don't believe it would distance the people where they are covered by the agreement.

Mr. **Bailey**. I would not want to be impolite and discourteous by responding that if you followed that logic, maybe you would want to come closer to the United States and be a State. I don't know. But I won't put you in that box.

I would say that I very much respect the position that you have taken and I want you to know as one member of Congress anyway that if I can help or assist in the wellbeing of the people there, it is very, very important and I think it is absolutely as important as any other American citizen anywhere.

I would have to study some of these ideas, and I don't know enough, I have to say that to you. But I thank you very much for coming today, and I very much respect the amount of detail that you have presented.

Mr. **Colberg**. Let me add one point. Mr. Ramirez spoke about the professor from Yale. They contend there are only two limitations for Puerto Rico entering into bilateral and multilateral agreements and those two limitations are national defense and political international relations. That power is reserved for Congress and the President.

Mr. **Bailey**. What you need are voting Congressmen and a couple of Senators up here. I thank you very much.

Chairman **Gibbons**. I am not as familiar with the constitutional problems as I would like to be concerning the relationship of

Puerto Rico and what you pointed out about there being two limitations, one for national defense and one for foreign affairs.

I have asked the staff to look into this because it would seem to me the better part of wisdom in dealing with the problems that are unique to Puerto Rico, a long way away and having an economy that is more like the island's than the mainland, would be to allow people of Puerto Rico to control their own destiny to the greatest extent possible. That much makes good horse sense, as we say.

So I would say any writings or opinions that you have on that I wish you would direct them to the staff here and we will see what can be done within the scope of this legislation to try to assist in that.

I recognize that your problems are unique, that you are a long way from this market, that you are caught in the Jones Act, and you are caught in a lot of other things that tend to make you at a disadvantage. I think it would be great if you can get Mexico and Venezuela to sell you oil cheaper, and you might set a good precedent. Certainly it wouldn't hurt anybody's economy if that happened.

I thank you very much for coming and participating in this. I commend you for the interest you have taken in this and I realize it is in your own self-interest, though.

The testimony or the report that is here, the economic report and testimony before your assembly will be made a part of this record.

Mr. **COLBERG**. We appreciate this opportunity, Mr. Chairman, in being here today.

Mr. **RAMÍREZ**. Thank you very much, Mr. Chairman, and thank you very much, Mr. Bailey.

Chairman **GIBBONS**. We are not going to be able to get to Mr. Roach today, but if you come in tomorrow we will take you at the end of the testimony and give you 10 minutes at that time.

Our last two witnesses for the day, or excuse me, we have three witnesses here, the Honorable Luis A. Ferre who is the senate minority leader, and the honorable Nicholas Nogueras, senate minority whip, and the honorable Angel Viera Martinez, house minority leader.

STATEMENTS OF HON. LUIS A. FERRE, SENATE MINORITY LEADER, AND HON. ANGEL VIERA MARTINEZ, HOUSE MINORITY LEADER, PUERTO RICO LEGISLATIVE ASSEMBLY

Mr. **FERRE**. Chairman Gibbons and members of the subcommittee, I am Luis A. Ferre, and during the years 1968–72 I served as Governor of Puerto Rico. Currently, I am pleased to serve in the senate as president of the New Progressive Party's delegation. I am also the chairman of the Republican Party in Puerto Rico.

Accompaning me today is Angel Viera Martinez, current floor leader of the new Democratic Party's delegation in the Puerto Rican House of Representatives.

Senator Nicolas Nogueras was to have been here, but an illness in his family prevented his making the journey. I ask that he be allowed to send his statement to you for inclusion in the record of this hearing.

Chairman GIBBONS. Yes, it will be included.

[The statement was not submitted.]

Mr. FERRE. I would like to insert the following comments: The fact that Mr. Martinez and I are here today is a direct refutation of the witnesses' statements where they come here and they say things reflecting the broadest base consensus of our people.

I am fully aware that this is not the place to discuss the international politics of Puerto Rico, but the fact is that the previous witnesses do not represent the Government of Puerto Rico, but rather a razor thin legislative majority which rests only on the peculiarities of the 1980 election. They were able to win, which, by the way, is still being contested in the Supreme Court.

This is not an opportunity to build a consensus on this issue, but as a means of endorsing party discipline I can personally attest to that since none of the positions I sent to them were included. This is equally true for the way we elected the Governor and covered the presentation here.

Despite what you have heard, an active consultation process has been going on between the Reagan administration, and Governor Romero, Governor Larla, and myself, and other parties in Puerto Rico, in an attempt to reach conclusions about the Caribbean Initiative in Puerto Rico.

This consultation has resulted in the recommendations presented to you by Congressman Corrada yesterday and the Honorable Jaime Benitez. With that in mind there are two reasons for being before you today. The first is to express our support for the purposes of the Caribbean Basin Initiative.

The second is to inform you of the problems which could arise should the suggestions raised by the previous panelists from Puerto Rico be adopted by the Congress. I refer specifically to the petitioning for the power to have Puerto Rico set tariffs, customs and tax rates on imported goods, and do so in place of existing Federal power in these areas while Puerto Rico remains part of the United States.

I should like to address myself, in a large part, to the first of our reasons for being here, and allow my colleague to address the second.

Puerto Rico is part of the United States, but our location, portions of our history, and our cultural links place us squarely in the Caribbean. As a result, throughout our history, Puerto Ricans have felt a moral obligation to serve the cause of freedom in the Caribbean. This combination of factors enriches life in Puerto Rico, and it also helps us understand clearly the problems facing the Caribbean nations today.

These are problems which neither dollars nor military assistance alone will solve. Indeed, an integrated approach, such as one set forth in the Initiative before you, is necessary. Not only is an integrated approach necessary using the tools of trade, aid and investment, but the approach calls upon the United States to use all the resources at its disposal to assist these nations in their drive for development.

One of these resources is the expertise built up in Puerto Rico over the past 30 years as we have used investment, trade and aid to develop the private sector, to solve infrastructure problems, to diversify our economy and to widen our industrial base. That is why I, and all Puerto Ricans, are pleased that the Initiative specifically mentions making use of Puerto Rican resources, just one of which is the tropical agricultural research facility located at Mayaguez.

Puerto Rico has other resources. We are a Spanish-speaking community with broad technical and managerial experience. Our educational standards are high, and our democtratic tradition long and deeply engrained. I may add that Jamaica has 5,000 university students out of a population of over 12 million, and Puerto Rico has over 150,000 university students out of 3 million.

These resources can be lent to our Caribbean neighbors for the assistance of all involved. But above even this is one more resource which will be of use to the United States. We are the symbol of the American democratic presence in the Caribbean itself.

The use of Puerto Rican resources will be of benefit to the island, but we are aware that the Initiative as it is implemented is not without risk to the economic health of Puerto Rico. We suffer from an unemployment rate of over 20 percent and as in most of the United States, our industries are running at less than full steam. Some of the same goods produced in Puerto Rico are produced throughout the Caribbean Basin: Rum being the foremost example.

Elimination of tariffs on this and other manufactured goods or agricultural products could cause problems for our island. While there still remain points on which to agree, the Reagan administration has already included, to use rum again as an example, provisions which protect both our industry and the revenues it generates. Governor Romero will, I believe, be addressing this point in his testimony tomorrow. But for the moment, let me say that I believe the Reagan administration is acting in good faith as it attempts to meet the special problems which the CBI may cause for Puerto Rico.

I have personally participated in discussions with the administration on this matter. Those appearing before us would have you believe that the only course to follow in addressing possible problems is to give Puerto Rico more and more privileges, resulting in a degree of autonomy unknown under the American system which is far different than the historical American tradition of granting territories powers that eventually will facilitate their entry into the union as States.

There is one clear solution to the problems of Puerto Rico and that is become a State of the Union. To them, the Caribbean Basin Initiative is a plan which literally forgets the "common" aspects of commonwealth. There can be no further proof of this than to note that their proposals in this area are identical to the notions recently advanced by the Puerto Rico Independence Party.

Before I turn to my colleague, who will speak more directly about some of the proposals you have heard, let me say that there are certain areas of agreement among Puerto Ricans regarding the Caribbean Basin Initiative and Puerto Rico. Many of the economic development measures suggested, such as the removal of the law which limits the stay of foreign cruise ships to 24 hours, are looked on favorably by all.

However, there is a large difference in the way we view the Caribbean Basin Initiative philosophically. We believe that this is an economic development package for the Caribbean which has economic implications for Puerto Rico.

If successful, the Initiative will help prevent the economic, and political, deterioration of the Caribbean Basin. The popular Democrats, on the other hand, view this as an opportunity to further their political interests irrespective of the economic impact on the island, on the rest of the Caribbean and on the United States. I think you will agree with me that a view like that can only harm our Nation's efforts to improve the social and economic well-being and political stability of the people of the Caribbean.

May I add that in trying to do this or develop this Caribbean Basin Initiative we might take advantage of requesting a part of the quid pro quo of these concessions that certain things be done in these areas which tend to give the people a higher standard of living. For example, we might require a minnimum wage floor in the Caribbean area that would participate in this free market in the United States and that would help to keep the costs of these products on a level with American production, and also fringes which would be given to these areas on the labor market that would help us to keep wages at a more reasonable level.

I think it would be very good because it will show that we are not only interested in having free trade and investment in these areas, but we will be trying to help the labor unions and the labor of the area to improve their standing in income. This would be of great benefit to the United States. You gentlemen can do both of these things at the same time. That is not only give them capital, but help labor to obtain a greater return for its work.

Chairman GIBBONS. Thank you, sir. We appreciate your statement.

Now, Mr. Martinez, you may proceed.

Mr. MARTINEZ. Mr. Chairman and members of the subcommittee, I am Angel Viera Martinez, and currently I serve in the House of Representatives in Puerto Rico as floor leader of the New Progressive Party's delegation. I was Speaker of the House during the years 1969–72. I served as minority leader from 1973–76. After the elections of that year, I again served as Speaker from 1977–80 and then again from April 1981 to the end of December 1981. I am also the chairman of the Democratic Party in Puerto Rico which is related to the National Democratic Party and I am a member of the DMC.

During these 3 days of hearings, according to your witness list, you will hear 43 separate witnesses. As a fellow legislator, I can well understand how time consuming these hearings can be, regardless of how worthwhile the subject matter. I, and Governor Ferre, would have been happy to shorten these hearings by even a little. Had there been agreement in Puerto Rico on the issues to be presented to you, a joint statement could have been prepared and delivered by one or two witnesses. But we were forced to come before you as a result of the actions of the panelists who have just concluded their testimony. This is said with all respect. But they would have you believe that the Caribbean Basin Initiative is an opportunity to address and perhaps alter the political status relationship between Puerto Rico and the United States.

We do not feel that way. The status debate is an ongoing process on the island of Puerto Rico. It has no business being addressed by this committee at this time. There are practical as well as political problems in granting the power shift requested by the previous panelists, and I will address them later.

Before I begin, let me say that there are many areas of agreement between the two panels in possible changes in the Caribbean Basin Initiative as it affects Puerto Rico. These, however, are suggestions which address economic issues, and not political ones. There is no agreement on the island regarding the political questions included in their testimony.

We support the aims of the Caribbean Basin Initiative. It is a high-minded attempt to address the problems of the Caribbean. We recognize that there may be problems for Puerto Rico within the context of the Initiative, but these problems are still being discussed between the Puerto Rican Government and the Reagan administration, and beginning tomorrow, between Governor Romero-Barcelo and yourselves. I would hope that you will not be distracted from the real issues by the statements of the previous witnesses.

Let me now turn to some of their statements.

These statements are found not only in the testimony just presented, but in a resolution passed in Puerto Rico over our objections. The purpose of the resolution, and indeed their testimony, was to petition you for the inclusion of certain measures pertaining to Puerto Rico and to ask that extraordinary powers be granted the Government of Puerto Rico; powers that no single state enjoys.

Some of the requests are good, and useful. These include: Eliminating the 24-hour limit on the stay of cruise ships in Puerto Rico, protection of our rum industry and the revenues it generates, expanding the air service between Puerto Rico and the rest of the world, using Puerto Rican resources to benefit the rest of the Caribbean especially in the areas of technical and higher education, something that I had mentioned last year to the White House Task Force on Puerto Rico, extending the accelerated cost recovery system to the island, and the protection of certain particular goods, such as vegetables, or industries, such as tuna canning, and pineapple on the island.

As you know better than I, many of these requests are already incorporated into the features of the Caribbean Basin Initiative. Some of them are still under discussion and may eventually be included in the legislation signed by the President to implement the Initiative.

Some of the requests, such as those relating to section 936 of the U.S. Tax Code, a block grant of Federal funds for Puerto Rico, the use of Puerto Rican industries as suppliers for Federal Government contracts, and the amending of the Jones Act as it applies to Puerto Rico may need to be addressed, but not as part of the Caribbean Basin Initiative.

But this is not the heart, the core, of their petition. The centerpiece is first, the granting to Puerto Rico the power to impose tariffs and other controls on the importation of products from foreign nations; second, allowing Puerto Rico the power to enter into bilateral or multilateral commercial, cultural, and sporting agreements with other nations, and third, granting Puerto Rico the power to control shipments from the United States as a means of protecting local production.

These three points go far beyond any measure yet suggested as a way of protecting the economy of Puerto Rico. Even the Governor of the Virgin Islands, who testified yesterday, and who clearly felt that the Caribbean Basin Initiative would be harmful to his islands, did not request additional powers to improve the situation.

Even if these powers would be granted to Puerto Rico, and Puerto Rico be made more sovereign than any State in the Union, there appears to me to be practical problems so evident as to make their implementation an impossibility. One example will suffice.

Should Puerto Rico feel the need to control shipments from the United States, what is to prevent the United States from doing the same to Puerto Rico? If the movement of goods can be controlled, it is but one step to the control over the movement of people.

I firmly believe that the ultimate granting of these powers would be disastrous for our island, and our Nation. They are directly opposed to the notion of common market, common currency, common welfare, common defense, and common citizenship on which the Commonwealth of Puerto Rico is based, before they defend, of course, we are for statehood and I might take this moment to make a remark to the effect that a gentleman from Pennsylvania, Mr. Bailey, said something about the change of status.

I would like to remind you of this. When the concurrent resolution was on the floor for debate, one of the leaders of their party, the Popular Party, and a representative, Mr. Jose Requires, Chairman of the Finance Committee, proposed an amendment to the second paragraph of the concurrent resolution, and it was rejected by my distinguished colleague and my dear friend, the Speaker of the House.

The second paragraph of the concurrent resolution was this, and I quote:

> To offset the harmful aspects of the Caribbean Basin Initiative and so that the objective for the benefit and prosperity may be attained, the legislature hereby appears before the Congress to claim the measures, the rights and the powers as specified herein below.

Then it proposed an amendment which was as follows, and I quote:

> All of them within the framework of the existing relationship and permanent association between Puerto Rico and the United States, and varies in the principle of common citizenship, and common courtesy and common defense and common market.

The Speaker, and this was all said with respect, objected and the amendment was defeated between them by a vote of 18 to 8 because we abstained.

The gentleman who answered the question made by the Honorable Congressman from Pennsylvania, had their position and of course I didn't intend to answer in this matter, but just there was a question, the gentleman who answered the question who is my dear friend and colleague, who is the Vice President of the Senate and Acting President of the Senate, Sergio Pena Clos, when he was asked if part of this proposal was that the Puerto Rican people form a nation, more or less, and he said "No." But very recently, as recently as January 2, 1980, he proposed that the U.S. court in Puerto Rico must disappear as a colonial relic, and I am quoting from the paper.

Mr. Chairman and members of this subcommittee, your time is being taken up by the previous panelists in a political attempt to have you address the question of the status of Puerto Rico and not of ways to assist the nations of the Caribbean.

Yesterday, Mr. Chairman, you stated that this subcommittee is not the forum for discussing the status of Puerto Rico. That is our view. We feel, that we should be here supporting the noble aims of the President's proposed policy and to do whatever we can as American citizens to further that aim.

In the past, we have served as soldiers, but we are just as pleased to serve as a resource, and as a center for expertise and knowledge on behalf of the United States to the rest of the Caribbean. It seems wrong to have you and the members of this subcommittee distracted from the real goals of this hearing by the statements of the other panel from Puerto Rico.

Thank you, Mr. Chairman.

Chairman **Gibbons**. Thank you, sir. I think you have pointed out some of the very tough political problems and practical problems we face in trying to pass this legislation and to try to do justice as best we can by the people of Puerto Rico.

Nothing of course in this legislation or within the jurisdiction of this committee affects the status of Puerto Rico. We merely try to untie the hands of you to get the most out of your economy that you can to raise your standard of living and not suffer unnecessarily or unknowingly at the hands of this Congress.

I appreciate the very fine statements you have made and the very well thought out positions you have taken. Puerto Rico is caught in a tough position. It is geographically in the Caribbean, but politically and to some extent economically within the United States.

I think that what we should try to do is try to solve the problem rather than to make it more difficult. There are enough difficulties already. We will be glad to work with you and your representative here in Congress who does a fine job. Your representatives here in the past have done fine jobs to try to sensitize us to the needs of paying special consideration to unique problems of your island territory.

Mr. **Martinez**. Thank you, Mr. chairman.

Mr. **Bailey**. Thank you, and welcome. We may just possibly agree 50 percent and disagree 50 percent, I am not sure. But be that as it may, I agree with what the Chairman has said. Although I cannot think that on either side there has been a real desire, or at least I hope not, to cloud the issue, I have to say that honestly I do have some serious questions about the Initiative and I really do. I have those very serious questions partially because I do wonder if we know enough about the way it is structured and the result and impact that it will have on Puerto Rico.

I have to raise those questions. I am curious if you have been able to evaluate the effect of the tax changes in particular. I am talking about the investment tax credit.

By the way, I was in error earlier today. I had commented on the accelerated depreciation portions of the Caribbean Basin Initiative and obviously had created the impression that the deduction, the availability of accelerated depreciation, the cost recovery system was going to be a part of the extension of the Initiative to the other Caribbean-based countries. It is not. It is only the investment tax credit.

So if I created that impression or made that illusion, I stand corrected. My fear, though, is it really doesn't change anything in terms of my analysis of my fears.

Have you been able to evaluate the net impact on Puerto Rico and particularly in the agricultural sector? We had some of those questions raised earlier today.

Mr. **Ferre**. I have not had a chance to evaluate that, but we are discussing that, and the Governor is discussing it with the administration to clear up many areas in relation to this.

Mr. **Bailey**. What about the effect of Puerto Rico and exports to other countries, that is Third World countries? Have you been able to evaluate the impact of the CBI on you in that regard? In other words potential conflicts or competitions between Puerto Rico and products of other CBI countries, or the CBI countries, the non-American countries affected?

Mr. **Ferre**. Yes, there may be an invitation for competition from other areas and I think we should stimulate our explanation to all of them.

Mr. **Bailey**. But you mentioned something very correctly, Mr. Martinez. You mentioned the competition with wage rates. Now we just had a fellow in here earlier today and I was questioning him on the real income impact, and I will check this out, but he alluded to a currency devaluation as a drop-off in real income for people in Costa Rica of about 10 or 15 percent who are receiving wages of 67 cents an hour that are possibly going to be doing the same things we have Puerto Rican people doing right now.

The Puerto Rican people are American citizens and they are just as important to us.

Mr. **Ferre**. I think since we are discussing the various impacts, there are still a lot of things that have to be cleared. What we do believe is that it is the duty of Puerto Rico to help the Caribbean Basin to improve, democratically and economically. That may take some complicated negotiations and some sacrifices at some time, but I think one thing we can do is to negotiate on the preference conditions with social improvements.

Mr. **Bailey**. You are talking my language now, and I am with you 100 percent. That is exactly the kind of approach in my opinion. I don't know how to structure it and I am not sitting here with technical language, but those are the kinds of things that would make it effective and meaningful to the average person down there, not just the presence of an American corporate structure or something like that. It is something that is going to mean something to the people in the street and people in the countryside and the villages.

Yes, sir, that is exactly the kind of thing. But you see, the Caribbean Basin Initiative does not have that.

Mr. FERRE. That is one thing that Congress can introduce and I think a part of this thing is something that can be negotiated. That is how can we have greater impact with the social structure. We want to have people in this country sympathize with the United States because we are trying to help them.

How are we to help them if we cannot improve the lot of the people down there?

Mr. BAILEY. Would you think some of the packages that we ought to be offering if we are going to offer trade incentives should include some kind of options that a consenting country has to make?

Sometimes a country has to make these concessions, to recognize the importance of industrial democracies and workers' rights and even things like the democratic issues we try to push. That is part of our culture that we share, that is a respect for due process and respect for law and those kinds of things.

Those countries have the rudiments, but I had a businessman say in support of what you have said, a businessman doing business in the Caribbean, that we are not going to accomplish anything unless we give them the infrastructure.

I don't see how the CBI does that much towards providing the infrastructure, how to export, and how to do business, and how to market and how to build and how to invest. That is instead of offering 67 cents an hour jobs. That is good and that is okay, but it doesn't solve the political issue. To me it doesn't.

But you people know the area better than I do and I have not spent that much time down there. The time I spent was in Panama and I am not very well educated as much as I should be, but I know poverty when I see it. I know alienated people when I see them, who don't feel they are a part of the system, and we have enough trouble in this country with some of those things.

Mr. FERRE. That is what I think, that if we introduce certain minimum requirements in these packages, we might start this movement of improving the conditions of the working people of the areas.

Mr. BAILEY. If you have any specific recommendations on them, I would love to see them because our analysis right now shows a loss of Puerto Rican jobs right now in a couple of industries, at least two or 3,000 jobs. I won't say you won't make them up elsewhere and I know advances have been made in high-skilled areas of Puerto Rico by the investment there.

Mr. FERRE. We would be glad to make specific suggestions. I made something of this sort 20 years ago.

Mr. BAILEY. I am glad to hear that and I would love to learn that.

Mr. Chairman, I thank you.

Chairman GIBBONS. We thank you, gentlemen, for coming today and we thank all of the Puerto Ricans for coming today. I know you have political differences on all of this, but let me commend all of you for the fine manner in which you all conducted yourselves.

Thank you very much.

This concludes our hearing for today and the subcommittee will resume its hearings tomorrow at 9:30 in the Rayburn House Office Building in room No. 2203.

[Whereupon, at 1:25 p.m., the subcommittee adjourned, to reconvene at 9:30 a.m., Thursday, March 25, 1982.]

CARIBBEAN BASIN INITIATIVE

THURSDAY, MARCH 25, 1982

House of Representatives,
Committee on Ways and Means,
Subcommittee on Trade,
Washington, D.C.

The subcommittee met at 9:30 a.m., pursuant to notice, in room 2203, Rayburn House Office Building, Hon. Sam M. Gibbons (chairman of the subcommittee) presiding.

Chairman Gibbons. Good morning, Ladies and Gentlemen.

Today we will complete the Trade Subcommitte hearings on the Caribbean Basin Initiative. Governor, we welcome you here. We will proceed first with Mr. Daniel Akaka, of the State of Hawaii. Mr. Akaka.

STATEMENT OF HON. DANIEL K. AKAKA, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF HAWAII

Mr. Akaka. Thank you very much.

Mr. Chairman, I appreciate the opportunity to address the subcommittee today on the issue of the Caribbean Basin Initiative. This proposal has generated great interest in Hawaii, and I thank you and the subcommittee for giving me this opportunity to testify.

I share the concerns expressed by the President in his speech before the Organization of American States on the economic and political crises in the Caribbean region. As the President said, "What happens anywhere in the Americas affects us in this country."

I am concerned by the effect of the Caribbean Initiative upon a program that the Congress enacted only last December, the domestic sugar program. Anyone familiar with the deliberations which led to the establishment of the sugar loan program in the 1981 farm bill knows our victory was not easily won. The result achieved was a barely adequate 17 cents-per-pound loan program for the 1982 domestic sugar crop.

The sugar loan program is designed to help keep a viable domestic sugar industry in business. It is designed to cushion the effects of large scale losses by sugar producers that occur during years when the world sugar price is depressed.

Last year is a perfect example of what can occur in the absence of a domestic sugar program. In Hawaii alone, the 330 growers of sugar cane lost a total of $83.5 million. The program is modest in comparison with other farm programs. As the average cost of production exceeds 23.5 cents-per-pound for beet sugar and 22.5 cents-per-pound for cane sugar, a loan program of 17 cents-per-pound offers protection from only the most catastrophic of losses.

The proposal to allow duty-free entry of an additional 1.26 million tons of sugar per year has sent shock waves through the domestic sugar industry. The announcement of the Caribbean Basin Initiative came just as the Department of Agriculture was formulating regulations to implement the loan program. The prospect of increased duty-free import of sugar when the world price of sugar remains at 12 cents-per-pound threatens to bring about the one thing that both the Department of Agriculture and the domestic producers of sugar desperately want to avoid Government purchases of sugar under loan.

We are now entering a period of marked decline in total sugar imports. For 1982, imports are projected to be 3.2 million tons, a decrease of 27 percent over 1981. At the same time that our total import needs are declining, duty-free imports will increase dramatically under the Caribbean Basin Initiative.

Had the President's initiative been in place in 1981, duty-free imports of sugar from all sources would have been 2.3 million tons, rather than the actual 1.3 million tons. Total import needs will continue to decline for the foreseeable future. As this occurs, duty-free sugar will become a larger and larger share of our imports.

The sugar program relies on the assessment of duties and fees on sugar imports in order to protect the domestic price. As the volume of nonduty-free sugar imports declines and there is a corresponding increase in duty-free imports, we soon reach a point where the domestic sugar price cannot be protected.

I believe that the duty-free imports of sugar under the Caribbean Initiative will substantially erode the administration's ability to protect the domestic price for sugar as required by law. The expected increase in duty-free imports has placed tremendous pressure upon the Department of Agriculture to consider reducing the level of the price support in ways that were never contemplated by Congress when the program was enacted. An example of this is the repayment of interest in the event of forfeiture.

I realize that the President's proposal includes safeguards for the domestic sugar program. Congress must make certain, however, that the administration has not only the ability but also the will to defend the sugar program. Assurances alone are not enough. Without a specific requirement that the administration invoke the safeguards in the bill when the program is in danger, the Department of Agriculture will be forced to pursue steps to reduce the possibility of forfeiture of sugar placed under loan.

I would like to offer one major recommendation, Mr. Chairman, to the subcommittee. We are all aware of the provision of the Caribbean Initiative to rebate excise taxes on all rum imported from Puerto Rico and the Virgin Islands. Consideration should be given to imposing duties on sugar from benefiting nations of the Caribbean Basin and then rebating these moneys to those governments. This would serve a number of useful objectives. First, it would assure that the benefits of duty-free import would be received by those who need it most—not the multinational corporations that own a majority of the sugar production resources in the region. Second, it would solve a related problem wherein a sizable share of the duty-free benefit may be retained by importers rather than the producing nation. This is because, under the administration proposal, the reduced price due to duty-free import will simply become another item of negotiation between exporters and importers. This will further dilute the level of benefit actually retained by the producing nation.

Finally, collecting duties and then rebating them to the producing nations would support the objective of discouraging greater economic dependence upon sugar in the Caribbean Basin. Diversification away from sugar is an important goal, but this can only be achieved if the incentive to increase sugar production is effectively removed.

Consideration must also be given to the developing tropical agricultural industries in areas such as Hawaii. Our climate is similar to that of the Caribbean Basin countries, and the Caribbean Initiative offers an incentive to the countries of the basin to expand production in crops such as pineapple, papaya, mangoes, and guava that are also grown and marketed by my State.

I am sure that all of agriculture would appreciate a guarantee that the administration will act swiftly to provide relief from excessive import of all types of competitive agricultural products. With the Nation's farm income at its lowest point since the Depression, farmers can ill afford to be undercut at the marketplace by duty-free import of agricultural products.

Mr. Chairman, this concludes my testimony. I hope you will keep my recommendations in mind as the subcommittee considers the Caribbean Basin Initiative.

I thank you very much for this opportunity to appear before you this morning.

Chairman GIBBONS. Thank you, Mr. Akaka. Let me ask you some questions about your plan to collect a duty and then rebate it.

What kind of duty are you talking about? Just elaborate on that a little more for me, please.

Mr. AKAKA. Presently, there is a duty of 2.1418 cents on imported raw sugar and 3.0014 cents per pound on refined sugar, important to our country.

Chairman GIBBONS. Yes.

Mr. AKAKA. This recommendation, it is to continue to charge duties on sugar important to our country, and these fees will be rebated to those governments or those nations from which these commodities come so that the nation itself will be benefiting, as I feel is the intent of the whole Caribbean Initiative.

Chairman GIBBONS. It would be a price-increasing mechanism on their sugar that was in effect rebated from the sugar and did not go to the owner of the sugar. Is that what you are describing?

Mr. AKAKA. That's right. Much of the sugar, of course, is being produced by multinational corporations. What I am suggesting is that the rebates would go back to the country from which these commodities come.

Chairman GIBBONS. That in effect would raise the price of imported sugar and tend to support the price of domestic sugar.

Mr. AKAKA. That's right. It would. But only to the extent that it is now being increased by the provision of the 1981 farm bill.

Chairman **Gibbons**. What kind of fee or tariff are you suggesting, the size of the fee or tariff?

Mr. **Akaka**. The amount would probably be commensurate with the fees and duties currently imposed under the present sugar program.

Chairman **Gibbons**. It would be like a European variable levy, if I understand it correctly, and would instead of being put in the U.S. Treasury, would be rebated back to the governments of the respective areas.

Mr. **Akaka**. That's right.

Chairman **Gibbons**. Are these multinationals that own the sugar in these countries, are they U.S. multinationals, are they foreign multinationals? Do you know?

Mr. **Akaka**. As I recall, there are some American-based multinational corporations.

Chairman **Gibbons**. Well, thank you. You have given us an idea to consider. I am also familiar with the problems of the tropical fruits, papayas, guavas. Some of the fruits we used to grow in my neighborhood, though for some reason it has gotten too cold to grow them in Florida unless you want to replant them every other year. But I know the problems in marketing those fruits. Thank you very much.

Mr. **Akaka**. Thank you, Mr. Chairman.

Chairman **Gibbons**. The next witness is the Puerto Rican Governor, and Mr. Corrada. Would you come forward with the Governor and introduce the Governor for us. We are most happy to have you here, sir.

Governor **Romero-Barcelo**. Thank you, Mr. Chairman.

Mr. **Corrada**. Mr. Chairman, I already testified in these hearings.

Chairman **Gibbons**. Yes, sir, and you did a fine job.

Mr. **Corrada**. Thank you very much. But it gives me today great pleasure to introduce to the subcommittee the Governor of Puerto Rico, Carlos Romero Barcelo. Governor Romero-Barcelo was recently elected 2 years ago to a second 4-year term. He is the first Governor in Puerto Rico in 20 years that has been reelected to a second term, his last three predecessors losing in that bid for a second term in our island. He was last year chairman of the Southern Governors' Conference, a distinguished member of the National Governors' Association, secretary of the Democratic Governors Association; and before being Governor of Puerto Rico, he was mayor of the city of San Juan and, as such, was very active in the National League of Cities, over which he presided in the year 1975.

So it is a great pleasure and honor for me to introduce and welcome Gov. Carlos Romero-Barcelo.

Governor **Romero-Barcelo**. Thank you.

Chairman **Gibbons**. Governor, we are happy to have you here.

STATEMENT OF HON. CARLOS ROMERO-BARCELO, GOVERNOR COMMONWEALTH OF PUERTO RICO

Governor **Romero-Barcelo**. Thank you.

I appreciate the opportunity to testify before the committee on the Caribbean Basin Initiative. At the outset, I would like to say that

Puerto Rico has been consulted extensively in the development of the Caribbean Basin Initiative, reflecting the administration's awareness of the importance of Puerto Rico in the implementation of the plan and its potential contributions to the economic development of the entire Caribbean Basin. As you well know, Puerto Rico is the only area of the United States that is within the Caribbean Basin itself. Puerto Rico strongly supports the Caribbean Basin Initiative's goals of economic growth for the Caribbean. Puerto Rico itself has advanced since World War II from a poverty-stricken island, heavily dependent on low-wage sugar production, to a modern industrialized economy, and we welcome the opportunity to share our expertise in this area with our neighbor—indeed, to become a major resource and center for banking, industry, agriculture, training and transport transportation for the entire Caribbean.

At the same time, we have expressed—and to a large degree the administration has shared—our concern that economic development for the rest of the Caribbean not be secured at the expense of Puerto Rico and the Virgin Islands. The Caribbean Basin Initiative proposal which you have before you contains most, but not all, of the safeguards that we have sought from the administration. For example, the bill extends the benefits of the accelerated cost recovery system and the investment tax credit to Puerto Rican companies, giving them some of the same tax incentives which are granted to mainland companies in last year's Economic Recovery Tax Act.

Other measures are being taken administratively to eliminate unnecessary barriers between the U.S. mainland and Puerto Rico and to put Puerto Rico on a more equal footing with the rest of the States. These include agricultural assistance, expanded air service to and from Puerto Rico, and the financing of vessels engaged in the transportation of goods from Puerto Rico to the mainland and vice versa. Still other measures are contained in separate legislative proposals.

In the interest of time, I will not go into detail in these areas today. A full discussion of the administration's commitments to Puerto Rico is contained in a prepared testimony which, with the chairman's permission, the committee's permission, I will submit later.

Chairman GIBBONS. Yes, it will be included in the record.

Governor ROMERO-BARCELO. Thank you. Today I would like to address primarily the economic impact of the Caribbean Basin Initiative on the entire Caribbean, including Puerto Rico and the Virgin Islands. I cannot stress too strongly the need to encourage economic development in the Caribbean Basin. Only through the strengthening of investment opportunities and the development of private enterprise can the nations in the Caribbean attain lasting progress. Puerto Rico offers the best example of what a Caribbean island can accomplish under a democratic, private enterprise system when individual initiatives are encouraged and supported. We are unique in that many of the same problems that Caribbean nations and islands are now addressing have been faced by Puerto Rico over the past 40 years. These include infrastructure creation, economic diversification and widening of our industrial base. We have done so within the context of a deeply ingrained democratic tradition. The expertise we have built up as a result of facing these challenges can serve the nations of the Caribbean well. It is a role Puerto Rico has historically played and one which can be greatly expanded as the Caribbean Basin Initiative moves forward.

I am concerned, however, that the initiative not destroy its principal model through one-way trade concessions in industries that can only hurt Puerto Rico. The broad purpose of trade reductions is good, since they will provide a major incentive for investment, production, employment, and trade for developing countries in the Caribbean. However, elimination of the tariff on processed canned tuna and rum poses a threat to our local tuna and rum industries, unless certain measures are taken.

Equally important, although Puerto Rico has made significant progress in economic development, it is still a developing area. Its per capita income, which has increased substantially over the past four decades, is still only half that of the poorest State in the Nation. Puerto Rico is an island almost entirely dependent on imports for its raw materials and exports for its sales and 90 percent of its offshore shipments go to the U.S. mainland. If the preferential access of Puerto Rico to the U.S. market is to be diminished by one-way elimination of U.S. tariff barriers—without equal consideration of Puerto Rico's circumstances—the island's ability to maintain an acceptable development rate would be seriously impaired at a time when we must greatly increase it.

I would like to discuss three areas in which the one-way trade concessions of the Caribbean Basin Initiative are particularly damaging to Puerto Rico. These are rum, tuna canning, and the various fruits and vegetables that Puerto Rico grows for export. I will discuss the problems raised by the Caribbean Basin Initiative in these industries in the order of their importance to Puerto Rico.

Rum is, of course, a vital concern to both Puerto Rico and the Virgin Islands, since they account for almost all of the U.S. production of rum. Puerto Rico alone accounts for 90 percent of U.S. rum production. Under current law, excise taxes on rum produced in Puerto Rico are rebated to the Puerto Rican treasury, providing more than 10 percent of Puerto Rico's annual budget. Puerto Rico's rum industry is particularly vulnerable to competition if elsewhere in the Caribbean Basin since Puerto Rico must import most of its molasses, the principal ingredient in rum. Stricter Federal and local labor and health laws and regulations in Puerto Rico, coupled with the requirements that Puerto Rican rum must be transported on U.S. ships, flag vessels, will encourage refiners to move their rum production to Caribbean Basin countries that have fewer restrictions and therefore lower costs.

To compensate for the elimination of tariffs on rum imported from elsewhere in the Caribbean, the administration's Caribbean Basin Initiative proposal provides for a rebate of all rum excise taxes, including those paid on rum from other countries, to Puerto Rico and the Virgin Islands. The bill also provides for additional compensation and safeguards if the rum industry in Puerto Rico and the Virgin Islands is damaged by the Caribbean Basin Initiative.

However, the rebate of excise taxes is only a partial solution to the problem. The transfer of money to Puerto Rico's treasury will be small comfort if the Puerto Rican rum industry is affected.

Most rum shipped from Puerto Rico and the Virgin Islands is shipped in bulk form, some rum is shipped in bulk from the Caribbean Basin countries as well. Therefore, this seems an appropriate place to start, since this is a sector of our rum industry that is particularly vulnerable to competition from other countries. Bottled rum has the benefit of brand identification. Bulk rum, on the other hand, is bottled on the mainland and could easily be produced elsewhere without any change in the habits of rum purchasers on the mainland. I therefore urge you to retain the tariffs on bulk shipments of rum into the United States. This will permit Puerto Rico to compete on an equal footing with other rum-producing countries. In addition, the snapback provisions of the bill should be strengthened to provide immediate relief if Puerto Rico's rum industry is threatened by imports. There should be an automatic reinstitution of tariffs, if Puerto Rican rum sales to the mainland drop below a certain level. I will be happy to work with you to develop a snapback provision that is both workable and effective, if that is the committee's wish.

TUNA

One industry in Puerto Rico which is threatened by the Caribbean Basin Initiative and can only be protected by retention of existing tariffs is tuna. Almost half of the total U.S. production of processed tuna is concentrated in Puerto Rico, particularly in the economically depressed south and southwest of the island. Tuna processing accounts for approximately 4 to 5 percent of Puerto Rico's manufacturing employment. Environmental restrictions on canning plants have required large expenditures. Elimination of the tariffs on tuna would encourage tuna processors to move their operations to countries with fewer environmental concerns, lower wages and resultingly lower costs. This would damage not only the Puerto Rican tuna industry, but the west coast tuna operations in the San Diego area. And we therefore urge this subcommittee to exclude processed tuna from the duty-free treatment of the Caribbean Basin Initiative.

Let me explain a little bit further all the disadvantages that we will be posed with in the tuna canning industry. Because we are covered by the Jones Act of 1920, Puerto Rico must fish all the tuna in U.S. flag vessels, and therefore, the wages for the fishermen, the wages for the crew are much higher than in foreign flag vessels. The U.S. flag vessels are more expensive to buy nowadays. The fuel costs are greater. So therefore, all of the costs of the fishing itself is greater. On top of that, you put together also the fact that their factory does not have to comply with the environmental concerns that we have to comply with in Puerto Rico, and it is a highly labor-intensive type of manufacturing industry and they can pay much more lower wages in the Caribbean Basin nations, therefore we are placed at a very, very serious competitive disadvantage.

OTHER INDUSTRIES

We are also concerned about a few commercial agricultural products which will be discussed in a lengthier and more detailed statement to be submitted with your permission. I refer to our being concerned with only a few because most of the agricultural products are not exempt; they don't pay any tariff from the Caribbean anyway. It is only a few of them we will be concerned with. For these products, safeguard measures should be strengthened to make it easier for producers to prove injury or the threat of injury from duty-free Caribbean imports. Measures should also be included to make it easier to obtain relief in the event of regional market disruptions such as the Puerto Rican market. The Caribbean Basin Initiative should include measures for an adjustment assistance program and an early warning system to identify threatened products before they are affected. Any such programs should include Puerto Rico.

A SEPARATE TARIFF REGIME

Puerto Rico's main opposition party has made proposals for solving some of the problems raised by the Caribbean Basin Initiative, many of which were included in our own recommendations. However, they have made several suggestions that would create serious trade problems for both Puerto Rico and the mainland. The opposition party has proposed that Puerto Rico set its own tariffs on imports and impose import restrictions on mainland agricultural shipments. They propose, of course, that free trade continue on exports to the mainland.

These measures run directly contrary to the long-standing "U.S. common market" which allows complete duty-free trade between the mainland and Puerto Rico. The GATT agreements, as well as other treaties, recognize the mainland and Puerto Rico as a single tariff territory. Setting up separate tariffs would encourage the inefficient production of commodities better imported from abroad and the mainland, and would penalize Puerto Rican consumers by forcing them to pay unnecessarily high prices for basic items. Furthermore, such a policy is contrary to the U.S. and international trade policy aimed at internal specialization and free trade. Imposition of a separate tariff regime for Puerto Rico would require approval by two-thirds of the GATT member countries or would require compensatory trade concessions to injured countries.

I don't know if the proponents are aware, but if we were to be granted the right to impose separate tariffs and we did impose them and we created injury to any of the signing countries, Puerto Rico would then be liable for compensation to those for damage created by the imposition of those special higher tariffs. Currently, Puerto Rico enjoys dutytree trade with the mainland and identical tariffs on imports from other countries. If Puerto Rico continued to enjoy this duty-free trade, while imposing different tariffs on imports from other countries, there would be a strong incentive for importers to ship goods first to the mainland at lower rates and then from the mainland to Puerto Rico duty-free. The problem would be reversed if the U.S. tariffs were higher than those in Puerto Rico. Additional documentation and recordkeeping would be necessary to prevent such transshipments. The opposition has obviously overlooked the possibility that separate and higher tariffs in Puerto Rico than in the mainland will affect Puerto Rico and will not only create ill will and resentment among Caribbean countries and islands, but would also provoke retaliatory measures. And I think the States of the Union, seeing how we have a special privilege imposing tariffs and those states not having it would create resentment against us and would put us in a very, very difficult position. Any time we came to Congress for something that was favorable to Puerto Rico, we would see resentment because of Puerto Rico's privileged position in the tariff situation.

Over and above its practical difficulties, separate tariffs and treaties run counter to the entire history of Puerto Rico's relationship with the 50 States. We should be striving toward a greater closeness and cooperation between the mainland and Puerto Rico. Additional divisive measures, such as those proposed by the opposition party, are inimical to the majority of both your constituents and ours.

PUERTO RICO'S MARITIME INDUSTRY

The opposition party has also suggested amending the Jones Act to eliminate entirely the requirement that goods traveling to or from Puerto Rico travel on U.S.-flag vessels. I have worked with the administration to improve air and sea transportation to Puerto Rico and to eliminate unnecessary restrictions. However, lifting the Jones Act cargo restraints entirely could damage Puerto Rico's state shipping industry—an industry which, contrary to our recommendations, the opposition party, when in office, purchased.

Some background is necessary to understand the problem. In an earlier administration, Puerto Rico purchased all shipping lines then serving the Puerto Rican mainland trade, and Navieras of Puerto Rico was born, a commonwealth-owned shipping line now. Puerto Rico incurred substantial debt to acquire the shipping lines and the Government's investment would suffer if increased competition cut into its volume of trade. I don't see how the Government can say we want foreign competition to come in and ruin our own industry, our own State-owned industry. It would not only hurt the Government directly, but will also mean the loss of jobs for U.S. citizens from Puerto Rico and the other States of the Union.

At the same time, there is no evidence that increased competition will provide any benefits to shippers. In fact, increased costs could be likely. Panama, for example, has not benefited from elimination of the Jones Act restrictions. Shipping between the United States and Panama now costs more than shipping from Hong Kong to the United States.

However, we do support measures that would extend the benefits under the Merchant Marine Act of 1936 to Puerto Rican carriers and shipyards. Title XI of that act, for example, requires that vessels financed by the United States must be constructed and repaired in the continental United States. This measure clearly discriminates against Puerto Rico and should be eliminated. We have to ship in U.S.-flag vessels; we can not ship in foreign-flag vessels. Why you would not be allowed also to repair vessels in Puerto Rico is beyond me. It is clear discrimination in the law. We also vigorously support measures to eliminate restrictions on passenger transportation to Puerto Rico. Puerto Rico is the only area within the Nation that does not have an alternative to air travel for citizens. We cannot travel any other way than by air. We have no way to use the car, the bus or the train, or the ocean lines, because there are no U.S.-flag vessels out of Puerto Rico. We are requesting, for example, that a passenger coming to and from Puerto Rico and the mainland be allowed to travel on foreign-flag vessels as long as there are no U.S.-flag vessels available. We don't see why it should not be—that exemption should not be granted.

Currently Puerto Rico is at a disadvantage with respect to the rest of the Caribbean. Travelers from the mainland cannot sail to Puerto Rico on a leisurely cruise and then return to the mainland by air, as they do in traveling to and from other Caribbean islands. Even if they go down to Venezuela and want to get off at Puerto Rico and give up the rest of the trip, they can't do it. There are criminal penalties. They have to get back on the ship.

If passenger travel were permitted on foreign vessels between the U.S. mainland and San Juan, travel to Puerto Rico would be more attractive to tourists from the mainland states. We also support elimination of the current restriction limiting cruise ships and their passengers to 24-hour stays in San Juan. These measures will help Puerto Rico to compete with other islands for tourists visiting the Caribbean.

CONCLUSION

In closing, let me reiterate my support of the Caribbean Basin Initiative. Although there are still details that need to be worked out to insure Puerto Rico's continued development, I believe that the Caribbean Basin Initiative offers major new opportunities for Puerto Rico to help itself and to help the basin. Carefully structured, the Caribbean Basin Initiative can only accelerate the development of the entire basin, including Puerto Rico. I will work with you, as I have worked with the administration, to fashion a workable Caribbean Basin Initiative that accomplishes these ends.

Thank you very much.

Chairman GIBBONS. Thank you. A very fine statement, Governor. And I commend you for the time and preparation you gave to it.

You know, there are a lot of things in the Trade Act that don't shock me any more because I know the history of them, but I am always shocked when I hear about the history of some of the things in the Jones Act and how it impacts upon you. And I will make a special request to the chairman of the committee that controls that Jones Act to see if we can't work out something to help in that. It sounds ridiculous not to be able to allow tourists to get off of a boat and fly back if that is the way they prefer it. I know many of them prefer that. A one-way sea voyage is all they want and they like to get off and fly back, or they like to fly there and get on and come back. And that has become pretty widely done. I know it is done in my own area. I see it quite often.

And the 24-hour requirement, I don't know where that one came from. We ought to really do something about that. I am going to ask the staff when they are going through that testimony to see if we can't get some cooperation out of the other committees to solve that problem.

Governor **Romero-Barcelo.** Thank you, Mr. Chairman.

Chairman **Gibbons.** I think you are on sound ground when you say we can't treat Puerto Rico as to tariffs any differently than we treat the other States of the United States. I know in my own area there would be clamors for keeping out vegetables from other parts of the world, maybe even from Puerto Rico, if we did that, because we can't compete with people in the vegetable and citrus area. I am already having some trouble with my citrus growers over all of this.

I wasn't really aware of your tuna industry. I know of the tuna industry out in American Samoa, and we have some particular problems out there. But I can see the problems that our environmental costs and our minimum wage cause you in competing in those areas. And the same in the rum situation. The Virgin Islands also has a bulk rum problem. In fact, their product is, as I understand it, all bulk rum, and apparently a large part of your production is bulk rum, too?

Governor **Romero-Barcelo.** Over half of the rum that we sell on the mainland is bulk rum.

Chairman **Gibbons.** And you suggest that we retain the tariff on the bulk rum and not worry about the competition.

Governor **Romero-Barcelo.** And some of that rum is bottled in Florida.

Chairman **Gibbons.** Yes, I know.

Well, you have made some good suggestions there, Governor. I am glad that the administration did consult with you. And I think it always puts you in a tough position to have the administration pushing you on one side and another group of people pushing you on another side. That is a rough job I guess all of us elected officials have. But——

Governor **Romero-Barcelo.** I was participating in discussions prior to taking a stand on the Caribbean Basin Initiative when I was asked, they said, "Now Governor, unless we give the Caribbean Basin countries the opportunity to have their agricultural products and their rum enter into the mainland without tariff barriers to help them help stimulate their economies, what other kind of thing can we do for them; can you give us a suggestion on that." I was put on a very difficult spot. I said no, there isn't. We feel it is extremely important that the nations and the islands in the Caribbean Basin be given an opportunity to stimulate their growth, their economic growth, and to strengthen their institutions, because the situation is difficult, extremely difficult, to say the least.

Chairman **Gibbons.** Well, I know we have a lot of poverty in the Caribbean Basin, and it is going to require a great deal of good luck and a lot of good planning to not do any damage to anyone as we try to remove that. And I think that is probably the main objective that Congress wants to have in all of this. We don't want to meddle in your internal affairs. We want to lighten the burden as much as we can from these changes. And we want to be attentive to what you wish. And I think above all, most Members of Congress don't want to get involved in the discussion that goes on in your island about well, should Puerto Rico be a State or should Puerto Rico be independent or should Puerto Rico continue on in its present status. As far as I am concerned, that is a decision for the Puerto Rican people to make after they have considered all the facts.

I would like to remove as many of the irritants as we can under the present system, and I think some of these you have outlined come under the heading of irritants. Perhaps we can work together and work those out.

Governor **Romero-Barcelo**. Thank you, Mr. Chairman.

Chairman **Gibbons**. Mr. Bailey.

Mr. **Bailey**. Thank you very much, Mr. Chairman.

Governor, we are happy to have you here. I noticed in your statement a slight note of caution beginning to creep in. I think all of us Americans share a very deep concern that what finally becomes the Caribbean Basin Initiative, if indeed it does end up being written into law, is that there be a primary concern for all of us, and all of us includes you. And I know that is your concern. And I agree with what the chairman said. We have got severe political problems down there. Poverty is very much a part of that difficulty, and we have got to find some way of encouraging investment there and increasing growth.

You know, you mentioned the history of Puerto Rico and the investment in effect that the mainland has made in Puerto Rico and the ties that now bind us so closely together. I couldn't agree with your reflection more, that they should not in any way be undone. I agree with you completely, and I encourage your attitude that way. I think that is excellent.

My fear is that the Caribbean Basin Initiative, because it is largely unexamined, does amount to some kind of net transfer from Puerto Rico and the Virgin Islands which really, when we look at the impact it will have on the political structure in the Caribbean Basin, won't accomplish very much. I have looked at that tax structure. I am particularly interested in the investment tax credit issue and I am very much a believer in using the tax code in that way. What it does is give an option to corporations to choose some of the benefits of existing law or, I should say, technically, as I understand it now, an accelerated cost recovery system and the investment tax credit. Have you sat down with the administration, have they given you a briefing on the net impact? For example, you stand to lose a few thousand jobs in the area, possibly in the leather or apparel or textile or the partial rubber industry. You know, some of those other areas could effect transfers, too.

Governor **Romero-Barcelo**. Apparel and textiles are excluded, but leather, yes.

Mr. **Bailey**. There are some fears that leathers and so-called rubberized or partially rubberized footwear are going to be affected also, and there are some jobs in Puerto Rico that are affected by that. You are a more experienced politician than I am. But because I know you have been through this before, you don't get jawboned to death by something that takes more from you than you build up.

You had some of your people working yesterday on wage rates, and I thought their ideas were excellent. One businessman mentioned to me transferring the infrastructure, the way to do business, how to do business, how to market, those kinds of things. Just by increasing the number of 60-some cent an hour jobs, for example, in Costa Rica, let's say, do we really do that much for that free enterprise system that is coming along so well in Puerto Rico and in the mainland, in which we believe? I don't know.

Governor **Romero-Barcelo**. Well, I believe, Congressman, that one of the important aspects of the Caribbean Basin Initiative, something I have insisted upon to the administration, that it is not only to try to stimulate economic growth, but also to help the countries and the islands help improve their health systems, their educational systems, their vocational training programs, the water distribution systems. In other words, there have to be direct services given to those areas to help them improve themselves and their infrastructure. If that is accompanied by the trade opportunities, it can accomplish quite a bit; it can go rather far in the next 10 or 20 years. The starting process is slow. Anything that is as bad off as some of those countries in the Caribbean Islands are right now can't be changed overnight. Any investor going down there will see the lack of infrastructure, the uncertainty of power, the needs for water, services, and the political instability in so many of the areas, and they will be very very leery about making any kind of an investment. I don't see that industrial investment is a real threat to Puerto Rico except in industries that are very, very basic, where the costs to set up a plant are minimal.

Mr. **Bailey**. I see it partly as a problem at home for you and at home for us here, because when you say to that American—I don't care if they live in Puerto Rico or they live in the mainland somewhere—you know, "Sorry, but your job goes. There is no skilled training for you, there is no money to move or relocate, I mean, you know, you are sacrificed." Because of the problems we have had with some of the prejudices on the mainland against Blacks and against Hispanics, which we all know have been a problem in our country that we have been working so hard to overcome, unfortunately, they are the people in some of these industries on the mainland who are most impacted. So I just want to share with you those fears and those cautions, and I thank you very much.

Governor **Romero-Barcelo**. I was going to say those fears and those concerns have not been addressed—I mean I don't think that any adequate study has been made, and I think it will be recommended that such a study be made so that we know what we are up against.

Mr. **Bailey**. We had an International Trade Commission witness before us and recommendations on notification and evaluations of job displacement were specifically written out of the law. That frightens me. That is just a bad faith thing to me, you know. And to seriously look at it and then write it out, I don't know why the administration did that, but I think it was very foolish. I can't understand why they would want to do it, what you would want to hide. But I still don't know why they did that.

But I thank you very much for an excellent statement. Thank you, Mr. Chairman.

Chairman **Gibbons**. Thank you, Governor

Governor **Romero-Barcelo**. Thank you, Mr. Chairman.

[The following was subsequently received:]

STATEMENT OF HON. CARLOS ROMERO-BARCELO, GOVERNOR OF PUERTO RICO

This statement supplements my testimony to this Subcommittee on March 25, 1982, in support of the Caribbean Basin Initiative (CBI). Puerto Rico has been consulted extensively in the development of the Initiative, reflecting this Administration's awareness of the importance of Puerto Rico in the implementation of the plan and its potential contributions to the economic development of the entire Caribbean Basin. Puerto Rico strongly supports the Caribbean Basin Initiative's goals of economic growth for the Caribbean. Puerto Rico itself has advanced since World War II from a poverty-stricken island, heavily dependent on low-wage sugar production, to a modern industrialized economy. We welcome the opportunity to share our expertise in this area with our neighbors -- indeed, to become a major resource and center for banking, industry, agriculture, training and transportation for the entire Caribbean.

MEASURES TO PROTECT PUERTO RICO

At the same time, we have expressed -- and to a large degree the Administration has shared -- our concern that economic development for the rest of the Caribbean not be secured at the expense of Puerto Rico and the Virgin Islands. The Caribbean Basin Initiative proposal which you have before you contains most, but not all, of the safeguards that we have sought from the Administration. Other measures are being taken administratively to eliminate unnecessary barriers between the United States mainland and Puerto Rico and to put Puerto Rico on a more equal footing with the states. Still other measures are contained in separate legislative proposals. I would like to take this opportunity, if I may, to summarize the Administration's commitments to Puerto Rico:

(1) Rum. To compensate for the duty-free status being afforded to rum imports from elsewhere in the Caribbean, the CBI provides for a rebate of all rum excise taxes to Puerto Rico and the Virgin Islands and other protections if our rum industry is damaged by CBI. United States Trade Representative negotiations will also seek commitments from Caribbean countries that they will continue to supply molasses to Puerto Rico and the Virgin Islands on commercial terms. While the Administration's proposal provides some measure of protection for the Puerto Rican rum industry, additional safeguards are necessary since this is an industry vital to Puerto Rico and one particularly vulnerable to imports. I will discuss the additional safeguards needed later today.

(2) ACRS and ITC. The President's proposal extends the benefits of the accelerated cost recovery system (ACRS) and the investment tax credit (ITC) to companies operating in Puerto

Rico and the Virgin Islands. This gives companies investing in new plants in Puerto Rico some of the same tax incentives granted to mainland companies in last year's Economic Recovery Tax Act.

(3) Puerto Rican Production. Under the CBI, value added to products in Puerto Rico will be considered in determining whether goods qualify for duty-free treatment. This will encourage companies to take advantage of Puerto Rico's more highly-skilled workforce for portions of their products requiring such skills, while utilizing lower-paid workers in other areas of the Caribbean for less-skilled work.

(4) Local Trade Safeguards. If additional Caribbean imports threaten the local market of any Puerto Rican industries, the Administration will consider assistance for those industries.

(5) Agricultural Assistance. The Department of Agriculture will extend rice price supports to Puerto Rico and will consider inclusion of Puerto Rico in all other price support programs covering commodities produced in Puerto Rico. We are also working with the Agriculture Department to extend the reinsurance program of the Federal Crop Insurance Corporation to Puerto Rico no later than mid-1983. These measures, plus increased technical assistance from the Agriculture Department, will help develop and improve the Island's agriculture.

(6) Petroleum Industry. Because of the critical importance of oil to the Puerto Rican economy, the United States

will make Puerto Rico a center for processing heavy crude oil, revitalizing Puerto Rico's refinery and petroleum industry. CORCO recently closed its heavy crude refinery and reopening this plant, Puerto Rico's largest refinery, will benefit not only CORCO but also several downstream petrochemical plants.

(7) Sea and Air Transportation. The Administration is committed to increasing sea and air transportation to and from Puerto Rico. Future bilateral negotiations will include expanded air routes between Puerto Rico and foreign countries, for both U.S. and foreign carriers. In addition, the Administration supports administrative changes that would permit cruise ships and their passengers to remain in San Juan for more than 24 hours. The Department of Transportation is studying its regulations affecting the cost of shipping for Puerto Rico, particularly in the area of rate setting and financing vessels.

(8) Environmental Regulations. The Environmental Protection agency will review the application of its rules to both Puerto Rico and the Virgin Islands and will endeavor to be more flexible in future applications of regulations impacting the islands.

(9) Puerto Rico's Role in the CBI. Most importantly, Puerto Rico will play a key role in the Caribbean Basin Initiative, serving as a resource center to the Caribbean Basin countries. Puerto Rico's history of industrialization, its

historic ties to the mainland, its bilingualism and its close connections to its Basin neighbors place it in an ideal position to provide technical assistance as Basin countries approach the United States market. Puerto Rico will serve as a hub in the Caribbean, a human and physical resource center. In addition, as the President indicated when he presented the CBI to Congress, the U.S. will foster integrated agricultural development of the Caribbean basin through increased research and training at the tropical agricultural research facility at Mayaquez, Puerto Rico.

I cannot stress too strongly the need to encourage economic development in the Caribbean Basin. Only through the strengthening of investment opportunities and the development of private enterprise can the nations of the Caribbean attain lasting progress. Puerto Rico offers the best example of what a Caribbean island can accomplish under a democratic, private enterprise system when individual initiatives are encouraged and supported. We are unique in that many of the same problems Caribbean nations are now addressing have been faced by Puerto Rico over the past forty years. These include infrastructure creation, economic diversification and widening of our industrial base. We have done so within the context of a deeply ingrained democratic tradition. The expertise we have built up as a result of facing these challenges can serve the nations of the Caribbean well. It is a role Puerto Rico has historically played and one which can be expanded as the Caribbean Basin Initiative moves forward.

ADDITIONAL MEASURES NEEDED

I am concerned, however, that the Initiative not destroy its principal model through one-way trade concessions in industries that can only hurt Puerto Rico. The broad purpose of trade reductions is good, since they will provide a major incentive for investment, production, employment, and trade for developing countries in the Caribbean. However, a damaging elimination of the tariffs on products important to Puerto Rico poses a threat to our local industries, unless certain measures are taken.

Equally important, although Puerto Rico has made significant progress in economic development, it is still a developing area. Its per capita income, which has increased substantially over the past four decades, is still only half that of the poorest mainland state. Puerto Rico is an island almost entirely dependent on imports for its raw materials and exports for its sales. Ninety percent of its offshore shipments go to the United States mainland. If the preferential access of Puerto Rico to the United States market is to be diminished by one-way elimination of United States tariff barriers -- without equal consideration of Puerto Rico's circumstances -- the Island's ability to maintain an acceptable development rate would be seriously impaired at a time when we must greatly increase it.

I would like to discuss three areas in which the one-way trade concessions of the Caribbean Basin Initiative are particularly damaging to Puerto Rico. These are rum, tuna canning and the various fruits and vegetables that Puerto Rico grows for export. I will discuss the problems raised by the Caribbean Basin Initiative in these industries in the order of their importance to Puerto Rico.

I. Rum

Rum is, of course, a vital concern to both Puerto Rico and the Virgin Islands, since they account for almost all of the United States production of rum. (Puerto Rico alone accounts for 90 percent of United States rum production). Under current law, excise taxes on rum produced in Puerto Rico are rebated to the Puerto Rican treasury, providing more than 10 percent of Puerto Rico's annual budget. Puerto Rico's rum industry is particularly vulnerable to competition from elsewhere in the Caribbean Basin since Puerto Rico must import most of its molasses, the principal ingredient in rum. Stricter federal and local labor and health laws and regulations in Puerto Rico, coupled with the requirements that Puerto Rican rum must be transported on United States ships, will encourage refiners to move their rum production to Caribbean Basin countries that have fewer restrictions and therefore lower costs.

To compensate for the elimination of tariffs on rum imported from elsewhere in the Caribbean, the Administration's Caribbean Basin Initiative proposal provides for a rebate of all rum excise taxes, including those paid on rum from other countries, to Puerto Rico and the Virgin Islands. The bill also provides for additional compensation and safeguards if the rum industry in Puerto Rico and the Virgin Islands is damaged by the Caribbean Basin Initiative. However, the rebate of excise taxes is only a partial solution to the problem.

Most rum shipped from Puerto Rico and the Virgin Islands is shipped in bulk form. This seems an appropriate place to start, since this is a sector of the rum industry that is particularly vulnerable to competition from other countries. Bottled rum has the benefit of brand identification. Bulk rum, on the other hand, is bottled on the mainland and could easily be produced elsewhere without any change in the habits of rum purchasers on the mainland. I therefore urge you to retain the tariffs on bulk shipments of rum into the United States. This will permit Puerto Rico to compete on an equal footing with other rum-producing countries.

In addition, the "snap-back" provisions of the bill should be strengthened to provide immediate relief if Puerto Rico's rum industry is threatened by imports. There should be an automatic reinstitution of tariffs, if Puerto Rican rum sales to the mainland drop below a certain level. I will be happy to work with you to develop a snap-back provision that is both workable and effective.

II. Tuna

Tuna is an industry in Puerto Rico which is threatened by the Caribbean Basin Initiative that can only be protected by retention of existing tariffs. Almost half of the total United States production of processed tuna is concentrated in Puerto Rico, particularly in the economically depressed South and Southwest. Tuna processing accounts for approximately 4 to 5 percent of Puerto Rico's manufacturing employment. Environmental restrictions on canning plants have required large expenditures. Elimination of the tariffs on tuna would encourage tuna processors to move their operations to countries with fewer environmental concerns, lower wages and resultingly lower costs. This could damage not only the Puerto Rican tuna industry, but the West Coast tuna operations in the San Diego area. We therefore urge this Subcommittee to exclude processed tuna from the duty-free treatment of the Caribbean Basin Initiative.

III. Commercial Agriculture

Puerto Rico is just beginning its transition to commercial agriculture, oriented towards export of tropical fruits and vegetables to the mainland market. Recently, my government has invested heavily in programs to grow new crops which were not formerly grown in Puerto Rico. In addition, I have proposed an exemption from Puerto Rican taxes for agriculture, to attract additional private investment in this sector of Puerto Rico's economy. In the past few years, agricultural employment in Puerto Rico has shown a tendency to grow, reversing a 30-year trend of declining agricultural employment. In the future, agriculture -- including processing -- could provide a much needed source of jobs on an island where the unemployment rate is 22.4 percent.

However, the introduction of one-way free trade would greatly hamper this self-help effort by allowing a variety of products which the government is trying to promote to enter Puerto Rico and the mainland duty-free. We object to elimination of the tariff on any agricultural item without a study of the effect of the tariff elimination on domestic producers of these items, including those in Puerto Rico. If tariffs are eliminated, based on such a study, they should automatically snap back to current rates if domestic production drops below the level shown in the study.

V. Other industries.

Equally important to both Puerto Rico and the mainland, safeguard measures should be strengthened to make it easier for domestic industries to prove injury or the threat of injury from duty-free Caribbean imports. Measures should also be included to make it easier to obtain relief in the event of market disruptions in regional markets such as Puerto Rico. The CBI should include measures for an Adjustment Assistance Program and an early warning system to identify threatened industries and plants before they are damaged and to help them become more competitive, produce new products, and save jobs. Any such programs should include Puerto Rico.

SEPARATE TARIFF REGIME

Puerto Rico's main opposition party has made proposals for solving some of the problems raised by the Caribbean Basin Initiative, many of which were included in our own recommendations. However, they have made several suggestions that would create serious trade problems for both Puerto Rico and the mainland. The opposition party has proposed that Puerto Rico set its own tariffs on imports and impose import restrictions on mainland agricultural shipments. They propose, of course, that free trade continue on exports to the mainland.

These measures run directly contrary to the long-standing "United States Common Market" which allows complete duty-free trade between the mainland and Puerto Rico. The GATT agreements, as well as other treaties, recognize the mainland and Puerto Rico as a single tariff territory. Setting up separate tariffs would encourage inefficient production of commodities better imported from abroad and the mainland, and would penalize

Puerto Rican consumers by forcing them to pay unnecessarily high prices for basic items. Furthermore, such a policy is contrary to United States and international trade policy aimed at internal specialization and free trade. Imposition of a separate tariff regime for Puerto Rico would require approval by two-thirds of the GATT member countries or compensatory trade concessions to injured countries.

Currently, Puerto Rico enjoys duty-free trade with the mainland and identical tariffs on imports from other countries. If Puerto Rico continued to enjoy this duty-free trade while imposing different tariffs on imports from other countries, there would be a strong incentive for importers to ship goods first to the United States at lower rates and from the mainland to Puerto Rico duty-free. (The problem would be reversed if United States tariffs were higher than those in Puerto Rico.) Additional documentation and recordkeeping would be necessary to prevent such transshipments. The opposition has obviously overlooked the possibility that separate and higher tariffs in Puerto Rico than in the mainland will affect Puerto Rico and will not only create ill will and resentment among Caribbean countries and islands, but will also provoke retaliatory measures.

Over and above its practical difficulties, separate tariffs and treaties run counter to the entire history of Puerto Rico's relationship with the 50 states. We should be striving toward greater closeness and cooperation between the mainland and Puerto Rico. Additional divisive measures, such as those proposed by the opposition party, are inimical to the majority of both your constituents and mine.

PUERTO RICO'S MARITIME INDUSTRY

The opposition party has also suggested amending the Jones Act to eliminate entirely the requirement that goods traveling to or from Puerto Rico travel on United States flag ships. I have worked with the Administration to improve air and sea transportation to Puerto Rico and to eliminate unnecessary restrictions. However, lifting the Jones Act cargo restraints entirely could damage Puerto Rico's state shipping industry -- an industry which, contrary to our recommendations, the opposition party, when in office, purchased.

Some background is necessary to understand the problem. In an earlier administration, under the opposition party, Puerto Rico purchased all shipping lines then serving the Puerto Rican mainland trade, and Navieras of Puerto Rico was born. Puerto Rico incurred substantial debt to acquire the shipping lines and the government's investment would suffer if increased competition cut into its volume of trade. This would not only hurt the government directly, but also mean the loss of Puerto Rican and mainland jobs.

At the same time, there is no evidence that increased competition will provide any benefits to shippers. In fact, increased costs are likely. Panama, for example, has not benefited from elimination of the Jones Act restrictions. Shipping between the United States and Panama now costs more than shipping from Hong Kong to the United States

However, we do support measures that would extend benefits under the Merchant Marine Act of 1936 to Puerto Rican carriers and shipyards. Title XI of that Act, for example, requires that vessels financed by the United States must be constructed and repaired in the contental United States. This measure clearly discriminates against Puerto Rico and should be eliminated. We also vigorously support measures to eliminate restrictions on passenger transportation to Puerto Rico. Currently, Puerto Rico is at a disadvantage with respect to the rest of the Caribbean. Travelers from the mainland cannot sail to Puerto Rico on a leisurely cruise and then return to the mainland by air, as they do in traveling to other Caribbean islands. If passenger travel were permitted on foreign vessels between the United States mainland and San Juan, travel to Puerto Rico would be more attractive to tourists from the mainland states.

We also support elimination of the current restriction limiting cruise ships and their passengers to 24-hour stays in San Juan. These measures will help Puerto Rico to compete with other islands for tourists visiting the Caribbean.

CONCLUSION

In closing, let me reiterate my support of the Caribbean Basin Initiative. Although there are still details that need to be worked out to ensure Puerto Rico's continued development, I believe that the Caribbean Basin Initiative offers major new opportunities for Puerto Rico to help itself and the Basin. Carefully structured, the Caribbean Basin Initiative can only accelerate the development of the entire Basin, including Puerto Rico. I will work with you, as I have worked with the Administration, to fashion a workable Caribbean Basin Initiative that accomplishes these ends.

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Ways and Means
Subcommittee on Trade

Office of the Governor
La Fortaleza
San Juan, Puerto Rico 00901

April 16, 1982

The Honorable Sam Gibbons
Chairman, Subcommittee on Trade
Ways and Means Committee
U. S. House of Representatives
2204 Rayburn House Office Building
Washington, D. C. 20515

Dear Chairman Gibbons:

When I testified before your Subcommittee on March 25, 1982, you asked that I provide you with any changes that I felt were essential to Puerto Rico. This letter contains those suggested amendments to the Caribbean Basin Economic Recovery Act (H. R. 5900). While I support the Caribbean Basin Initiative proposed by the Administration, certain changes are necessary to ensure that economic development of the rest of the Caribbean is not obtained at Puerto Rico's expense.

At the same time, I have deliberately kept Puerto Rico's "wish list" to the minimum necessary to protect critical industries. For example, Puerto Rico is not seeking protection for its growth industries, such as electronics and pharmaceuticals, since these industries will provide ample opportunities for the entire Caribbean that can only benefit Puerto Rico. Instead, we seek full or partial protection for more traditional industries - rum, tuna processing, and agriculture - whose growth elsewhere in the Caribbean could be at our expense.

The following are the changes necessary to the Caribbean Basin Economic Recovery Act:

(1) Rum. Duty should be retained on bulk imports of rum. In addition, there should be a return to current tariffs if the market share of either Puerto Rico or the Virgin Islands is reduced below current levels.

The Honorable Sam Gibbons
April 16, 1982
PAGE TWO

(2) Processed tuna. Duties should be retained on processed tuna.

(3) Agricultural products. Before tariffs are eliminated on any perishable agricultural product, the Secretary of Agriculture should conduct a study of the impact of duty-free treatment on domestic producers, including those in Puerto Rico. Duty would be elimintated only if the Secretary finds that domestic producers will not be harmed. The Secretary would establish a level of domestic production for each month of the year. If sales by domestic producers fall below this level, the current tariff would immediately be reimposed, with a procedure for foreign producers to show that the drop in sales by domestic producers is not attributable to duty-free imports from the Caribbean.

The reason for each of these proposals is discussed in the attached supporting papers. Suggested legislative language appears in the last section.

Please feel free to contact me if you have any questions concerning either my proposals or the draft language. I will be pleased to provide any additional assistance or information that you need.

Sincerely,

Carlos Romero Barcelo

Carlos Romero-Barceló

Enclosures

RUM

Proposal

Duties on bulk rum (that is, rum imported in containers over one gallon) should be continued. In addition, there should be a snap-back to current tariffs on bottled rum (containers of one gallon or less) if the total market share of either Puerto Rico or the Virgin Islands in bulk and bottled rum is reduced below current levels.

Explanation

Rum imported into the United States is currently divided into two categories: rum in containers of one gallon or less ("bottled rum") and rum in containers over one gallon ("bulk rum"). The duty in both catagories is the same, $1.66 per gallon. Barbados currently receives duty-free treatment on bottled rum. In 1981, 84 percent of foreign rum was imported in bulk. Jamaica, Barbados, the Dominican Republic, Haiti and French West Indies are the principal exporters of rum to the United States.

Protection of its rum industry has been one of Puerto Rico's highest priorities in the Caribbean Basin Initiative. Federal excise taxes on rum produced in Puerto Rico are currently returned to the Island, accounting for approximately 10 percent of the Puerto Rican government's annual budget. In its proposal, the Administration has recognized the importance of rum to both Puerto Rico and the Virgin Islands by providing that excise taxes collected on foreign rum be rebated to Puerto Rico and the Virgin

Islands to the extent that their own exports to the United States mainland are reduced. However, this alone will not assure the continued vitality of the Puerto Rican and Virgin Island rum industries. The rebate of excise taxes from foreign rum provides some compensation for injury to our rum industries, but does little to prevent the injury in the first place.

Although Puerto Rico currently produces 90 percent of the rum consumed in the United States, the Puerto Rican rum industry is particularly vulnerable to competition from neighboring Caribbean Islands. At the present time, tariffs on rum help to minimize the difference in the cost of producing rum in Puerto Rico and producing rum in other areas of the Caribbean. Other Caribbean Islands have lower labor costs, since they do not have minimum wage laws comparable to those in the United States (which apply equally to Puerto Rico and the States). In addition, rum producers in those countries are not faced with the myriad of federal regulations concerning health, safety, and the environment that increase costs for domestic producers. The cost of rum production in Puerto Rico has been affected by environmental regulations that have necessitated expensive modifications in the treatment and disposal of rum effluent.

In addition, Puerto Rico is dependent on imports for much of the molasses used to produce rum, while other Caribbean countries rely on domestic sources of molasses.

Rum shipped in bulk is more susceptible to competition from other Caribbean producers than bottled rum. Bulk rum, which constitutes about 60 percent of the rum shipped from Puerto Rico to the mainland, lacks brand identification. A mainland bottler could shift rum production from Puerto Rico to another Caribbean Island without any change in the rum-buying habits of consumers. Duty-free exports to the mainland may be particularly attractive to countries that currently supply Puerto Rico with its molasses.

For example, rum imports from the Dominican Republic (a major producer of molasses) have been increasing in recent years. Imports from the Dominican Republic increased 167 percent between 1980 and 1981, all imported in bulk. The Dominican Republic would be in an ideal position to lure away part of Puerto Rico's rum business if tariffs are lifted, since it already produces both molasses and rum. Haiti and Trinidad also produce both rum and molasses. Duty-free treatment for rum could provide an incentive for these countries to convert their molasses to rum, which in turn would result in greater competition for Puerto Rico's rum industry.

The rum industry is not a significant source of employment. Thus, eliminating rum duties would not provide a significant increase in employment in the Caribbean. Any increase that did occur, however, would come at the expense of the Puerto Rican workers now employed in the rum industry.

In addition to maintaining the duty on bulk rum, the Caribbean Basin Economic Recovery Act should include a snap-back of the current duty on bottled rum if the market share of either Puerto Rico or the Virgin Islands drops below the current level. Puerto Rico is confident that its bottled rum can compete on an equal footing with imported bottled rum, even without tariff protection. However, granting duty-free treatment only to bottled rum could create an incentive for other countries to shift from bulk rum to bottled rum for export to the United States. This is particularly true of countries like Jamaica that already produce large quantities of both. To ensure that such a shift does not occur at the expense of Puerto Rico or the Virgin Islands, duties on bottled rum should be reinstituted if the total market share (bottled and bulk combined) for either Puerto Rico or the Virgin Islands drops below the 1981 level.

PROCESSED TUNA

Proposal

Section 103(b) of the proposed Caribbean Basin Economic Recovery Act should be amended to exclude tuna, prepared or preserved in any manner in airtight containers ("processed tuna"), from the articles eligible for duty-free treatment under the Act.

Explanation

Under Section 103 of the Caribbean Basin Economic Recovery Act, all articles produced by Caribbean Basin countries, other than textiles and apparel (which are excepted by Section 103(b) of the Act), would be eligible for import into the United States without payment of duty. The purpose of this proposal is to stimulate the economies of Caribbean Basin countries by making the U.S. market available to them on a duty-free basis. While we support this goal, we urge that it not be achieved at the expense of Puerto Rico. We fear that the duty-free import of processed tuna produced in Caribbean Basin countries would have an adverse effect on Puerto Rico's tuna processing industry. Accordingly, to preserve this industry, as well as the jobs it provides, we seek to retain the present tariffs and quota on the import of processed tuna.

Under the present system, processed tuna packed in oil is subject to an ad valorem duty of 35 percent (TSUS No. 112.90). In contrast, the rate of duty on processed tuna packed in water depends on the aggregate amount imported in any one calendar year. Up to 20 percent of the U.S. production of processed tuna packed in water in the prior year may be imported at an ad valorem duty of 6 percent (TSUS No. 112.30). Any amount over 20 percent, however, is subject to an ad valorem duty of 12.5 percent (TSUS No. 112.34).

This tariff and quota system for processed tuna, in conjunction with the absence of tariffs or quotas on the import of fresh, chilled, or frozen tuna (TSUS No. 110.10), has stimulated the development of the U.S. tuna processing industry. The U.S. is the second largest producer of processed tuna in the world. In 1980, domestic firms produced over 90 percent of all of the processed tuna sold in the U.S. More importantly, from our perspective, tuna processing plants in Puerto Rico produced over 40 percent of the processed tuna produced in the U.S.

Tuna processing is one of Puerto Rico's most important industries. In 1980, Puerto Rico shipped over $380 million worth of processed tuna to the mainland. These shipments represented approximately 7 percent of all of Puerto Rico's shipments to the mainland. Tuna processing also is one of Puerto Rico's largest employers. There are five tuna processing plants in Puerto Rico. All of them are located in areas which traditionally have experienced very high levels of unemployment. Together, the five plants employ approximately 7800 persons. These jobs represent over 25 percent of the manufacturing employment in the towns in which the plants are located, as well as over 4 percent of Puerto Rico's total manufacturing employment.

Elimination of the present tariffs and quota on processed tuna would threaten both Puerto Rico and the mainland (particularly California) with the loss of their tuna processing industries. This danger arises principally from the higher labor and regulatory costs associated with operating in Puerto Rico or on the mainland. Many of the employees of tuna processing plants in Puerto Rico and the continental U.S. are unionized. Moreover, all of them have the benefit of minimum wage and occupational health and safety laws and regulations. Further, tuna processors in Puerto Rico and on the mainland are subject to stringent environmental standards. For example, in 1977, three Puerto Rican tuna processors were required to build a waste treatment facility at a cost of over $1 million to meet federal effluent requirements. Moreover, these same three firms annually pay over $500,000 to operate that facility.

Although hard evidence is lacking (largely because of the failure of Caribbean Basin countries to keep accurate statistics), it seems quite safe to assume that tuna processors in many Caribbean Basin countries would not be subject to similar requirements. Accordingly, since operations in such countries would be less costly, many existing tuna processors and all new tuna processors would have an inducement to locate their plants in the Caribbean Basin if the present tariffs and quota were eliminated and the U.S. market was, thus, made available to them.

The real nature of this danger recently was recognized by the Office of the United States Trade Representative. Under the Generalized System of Preferences ("GSP"), 19 U.S.C. §§2461-2, the President is authorized, among other things, to extend duty-free treatment to articles imported from developing countries. Pursuant to the GSP, and the regulations implementing it, the governments of Malaysia and Morocco petitioned the Trade Representative's Office to extend duty-free treatment to processed tuna packed in water in excess of the quota.

After receiving submissions from interested parties establishing that elimination of the duty would make it uneconomical to process tuna in Puerto Rico or on the mainland, and that the tuna processing industry might, therefore, be forced to shift its operations to lower cost foreign countries, the GSP Subcommittee of the Trade Policy Staff Committee, a division of the Trade Representative's Office, denied the Malaysia/Morocco petition. 46 Fed. Reg. 28779, 28784 (May 28, 1981).

In summary, tuna processing is one of Puerto Rico's most important industries, both in terms of the dollar value of the product it produces and the number of jobs it provides. Moreover, because of the higher labor and regulatory costs associated with operating within the customs territory of the

U.S., the competitiveness of this industry depends in part on the continued existence of the present tariffs and quota on processed tuna imported from foreign countries. Elimination of this tariff and quota system would threaten Puerto Rico with the loss of its tuna processing industry and the jobs it provides, as in the absence of tariffs and the quota, the lower labor and regulatory costs of Caribbean Basin countries would lure tuna processors away from Puerto Rico. To avoid these problems, we seek to exclude processed tuna from the articles eligible for duty-free treatment under the proposed legislation.

COMMERCIAL AGRICULTURE

Proposal

Before tariffs are eliminated on any perishable, agricultural product, the Secretary of Agriculture should conduct a study of the product to determine the impact of duty-free treatment on domestic producers, including those in Puerto Rico. Only if the Secretary finds that domestic production will not be adversely affected, should tariffs be eliminated on a product. As part of the same study, the Secretary should establish monthly sales levels of domestic produce, based on the sales for the last full year (or on a historical average if that better reflects domestic production). If sales of domestic products fall below these levels in any month, the current tariff should immediately be reimposed ("snap-back").

Explanation

Puerto Rico is just beginning its transition to commercial agriculture, oriented toward exporting tropical fruits and vegetables to the mainland. The government has invested heavily in programs to grow new crops which were not formerly grown in Puerto Rico, including a large experimental effort in private-sector vegetable growing on the South Coast. Agricultural employment has been growing in the past few years, reversing a 30-year trend of employment declines in this sector.

We are concerned that the Administration has proposed one-way free trade on almost all agricultural products without any detailed analysis of the impact of this tariff elimination on domestic producers. Farming is a segment of the economy that is particularly susceptible to price fluctuations. The extent of competition in a given product market and the sensitivity of consumer demand to changes in price will vary according to product, so that a slight price increase can have a more adverse impact on one agricultural product than on another.

The Administration's proposal contains an expedited procedure for establishing injury to domestic agricultural producers. However, this test places the burden on the domestic producers to establish that duty-free imports from the Caribbean have caused the damage to domestic production. In its place, we propose an automatic snap-back of current duties which can be lifted on a showing by Caribbean producers that the injury was not caused by duty-free imports from the Caribbean. Once injury to domestic producers has been established, the burden would be on those who benefit from one-way free trade to show that duty-free treatment of Caribbean products is not the cause of the injury.

The trigger for the snap-back mechanism must respond quickly to changes in the agricultural marketplace, given the seasonal nature of agriculture. The current tariff system recognizes this seasonality, imposing higher tariffs on some agricultural products such as melons and tomatoes during the domestic growing seasons. Monthly comparisons should give immediate warning of instrusion by Caribbean imports into the domestic market share. The snap-back would then protect domestic growers until the Secretary of Agriculture can determine whether the decline in domestic sales is caused by some factor other than Caribbean imports.

RAMSEYER OF SUGGESTED CHANGES IN THE CARIBBEAN BASIN ECONOMIC RECOVERY ACT

(1) Rum and Tuna. Amend Section 103(b) to exclude bulk rum and processed tuna from the articles eligible for duty-free treatment, as follows:

"(b) The duty-free treatment provided under this title shall not apply to:

(1) textile and apparel articles which are subject to textile agreements;

(2) rum shipped to the United States in containers over one gallon; or

(3) tuna, prepared or preserved in any manner, in airtight containers."

(2) Perishable Agricultural Products. Replace the expedited injury procedures in Section 103(e) (shown in brackets) with a new subsection requiring a study before duty-free treatment is granted and a snap-back if sales by domestic producers decrease:

["(e)(1) If a petition is filed with the International Trade Commission pursuant to the provisions of section 201 of the Trade Act of 1974 regarding a perishable product and alleging injury from imports from beneficiary countries, then the petition may also be filed with the Secretary of Agriculture with a request that emergency relief be granted pursuant to paragraph (3) of this subsection with respect to such article.

(2) Within 14 days after the filing of a petition under paragraph (1) of this subsection:

(A) if the Secretary of Agriculture has reason to believe that a perishable product from a beneficiary country is being imported into the United States in such increased quantities as to be a substantial cause of serious injury, or the threat threof, to the domestic industry producing a perishable product like or directly competitive with the imported product and that emergency action is warranted, he shall advise the President and recommend that the President take emergency action; or

(B) the Secretary of Agriculture shall publish a notice of his determination not to recommend the imposition of emergency action and so advise the petitioner.

(3) Within 7 days after the President receives a recommendation from the Secretary of Agriculture to take emergency action pursuant to subparagraph 2 of this subsection, he shall issue a proclamation withdrawing the duty-free treatment provided by this title or publish a notice of his determination not to take emergency action.

(4) The emergency action provided by subparagraph 3 of this subsection shall cease to apply (1) upon the proclamation of import relief pursuant to section 202(a)(1) of the Trade Act of 1974, (2) on the day the President makes a determination pursuant

to section 203(b)(2) not to impose import relief, (3) in the event of a report of the United States International Trade Commission containing a negative finding, on the day the Commission's report is submitted to the President, or (4) whenever the President determines that because of changed circumstances such relief is no longer warranted."]

"(e)(1) The duty-free treatment provided under this title shall not apply to any perishable products unless the Secretary of Agriculture --

(A) conducts a study to establish the amount of such product which is sold by domestic producers on a month-by-month basis; and

(B) based on such study, determines that the duty-free treatment of such product is not likely to harm the domestic industry producing such product.

(2) If there is domestic production of any perishable product that is granted duty-free treatment under this title, the Secretary of Agriculture shall conduct monthly studies of such product by domestic producers. If in any month the amount of any perishable product sold by domestic producers is reduced below the level of domestic sales for that month of the year, as determined in the study conducted by the Secretary of Agriculture under paragraph (1), duty on such product shall be restored immediately to its current level.

(3) If duty on a perishable product is restored under paragraph (2), a foreign producer may petition the Secretary of Agriculture for a determination that the decrease in domestic market share was not caused by duty-free imports from a beneficiary country. If the Secretary makes such a determination, duty-free treatment shall be restored.

[(5)] (4) For purposes of this subsection the term "perishable product" shall mean --

(A) fresh or chilled vegetables provided for in TSUS items 135.10 through 138.42;

(B) fresh mushrooms provided for in TSUS item 144.10;

(C) fresh fruit provided for in TSUS items 146.10, 146.20, 146.30, 146.50 through 146.62, 146.90, 146.91, 147.03 through 147.33, 147.50 through 149.21, and 149.50; and

(D) fresh cut flowers provided for in TSUS items 192.17, 192.18 and 192.21."

(3) Rum Snap-back. Add a new subsection (f), containing a snap-back provision for duties on bottled rum, to Section 104:

"(f) The duty-free treatment provided under this title shall not apply to rum imported in containers of one gallon or less if the share of the United States rum market maintained by either Puerto Rico or the Virgin Islands is reduced below the market share maintained by such Commonwealth or possession in 1981."

Chairman GIBBONS. The next witness is our colleague, Mr. Cecil Heftel, a distinguished Member of Congress and a member of this committee. Mr. Heftel, we recognize you, and you may proceed as you wish.

Mr. HEFTEL. Thank you, Mr. Chairman. I would ask unanimous consent to have my full statement placed in the record, and I will summarize it as briefly as possible.

Chairman GIBBONS. It will be placed there in its entirety.

STATEMENT OF HON. CECIL (CEC) HEFTEL, A REPRESENTATIVE IN CONGRESS FROM THE THE STATE OF HAWAII

Mr. HEFTEL. Just recently we shared an evening on our export task force, and I was interested in your remarks to the group, which were consistent with the position I think you have always taken, that is, an enlightened and understanding approach toward free trade, recognizing the need for the United States to encourage world trade, and, in particular Caribbean trade.

Today, I want to share my concern, though, about what is happening in Hawaii. We have done this before. I will try to be brief. We have just witnessed the closing down of some 16,000 acres of sugar production, resulting in some 500 to 600 lost jobs with no replacement employment available. For these islands as a whole, we have about 9,000 jobs directly tied to sugar—now about 8,400. We have got something over 20,000 indirect jobs. And again we have no alternatives, because our soil just simply is not usable for a variety of other farm commodities.

Our pineapple industry has decreased by about one-third in the last 10 years, and we are now striving to build some new industries, papaya and sweet ginger, but those are very fragile because of the competition from not only the Caribbean but other areas of the world as well. But specifically I wanted to look at something that came to my attention in this past week. Anthuriums are a modest export from Hawaii which we sell at about 20 cents each to the wholesalers on the mainland. Jamaica is selling those in competition now for 3 cents. And when I spoke with our representatives about it, they said, well, ours are superior. But what we are running into now is people saying, well, with a margin of 3 to 20 cents, we can do with less quality and do a lot better financially by substituting Jamaican anthuriums for Hawaiian anthuriums.

Knowing your commitment to free trade, I hope as we go forward, tying in to some of the things Mr. Bailey has just said, that we look at the impact of the CBI on our domestic employment and our domestic industries. I know the great threat to Hawaii. I know the nervousness of the people because we don't have alternatives. And I am concerned that the administration, in its efforts to promote good relations in the Caribbean area, may not adequately look at the impact of its program on the United States and some of its domestic interests. But it is quite obvious that when we lose these jobs, as I see it in Hawaii, we create a new class of poverty in the United States where there is no alternative employment, where these people become outcasts in their own society. As they suddenly have no alternative means of employment, they are caught in a vicious cycle of poverty. And so it is in this light that I share my concerns, and would be delighted to entertain your thoughts and your questions.

Chairman GIBBONS. Well, I am sorry to hear about the closing down of the sugar industry in Hawaii. Is this land being used for any other purpose?

Mr. HEFTEL. Well, Mr. Chairman, these lands are owned either by major landowners or the corporate structures that are in the sugar business to start with, and they will find economic alternatives for themselves as a company and will find some kind of ultimate use for the lands. But there is nothing as an alternative for crop use. We have a very unusual soil situation in Hawaii; it just doesn't lend itself to alternate crop use.

One other observation should be made. Much of the sugar industry is owned by either conglomerates or multinational corporations, and in certain instances, they own comparable types of production companies in the Caribbean itself. We have no way of knowing whether these companies will end up with a higher level of profit, producing with free access to the American market and low-cost production in the Caribbean and subsequently phaseout, let's say, Hawaii operations. And so that is still another concern that we have. But the companies themselves are not what I am talking about. The fact they may lose $80 million this year tells us they are not going to continue the status quo. And we are not going to have employment for those people because that land is not usable for alternatives.

Chairman GIBBONS. The reason why I asked that is because in Florida we are constantly turning over dairy farms and citrus groves as the economics of the situation changes. If the tax would get too high or other costs get too high, the dairy or the grove becomes unproductive. It is a part of the natural economic process. Sometimes the most money a dairy man makes out of his dairy is when he disposes of it rather than when he operates it as a dairy. I just wondered if that was going on in Hawaii.

Mr. HEFTEL. It is a totally different situation. The 6,000 people who might not have jobs if there were a cessation of agricultural production have no access to employment in alternatives industries. There is no immediate use for that land. In other words, it isn't the kind of land that you would be able to subsequently develop. It isn't the sort of thing that you are experiencing in Florida. And the benefits—if there is a conversion—are totally unrelated to the employees. And on neighbor islands in Hawaii, there isn't alternative employment, so that when you stop production, you end employment and offer no alternatives. And these are people who are not well suited to leaving those neighbor islands to go anywhere to do anything else.

Chairman GIBBONS. What makes it more expensive to raise sugar on Hawaii than anywhere else?

Mr. HEFTEL. Well, we are fairly efficient in Hawaii in relation to the mainland. We can't compete with foreign production, particularly if it is sold below the cost of production. But we are also subject to very high cost of land in Hawaii.

Chairman GIBBONS. High cost of land, did you say?

Mr. HEFTEL. High cost of land. In other words, the land in Hawaii has a higher intrinsic value and cost than does land in other areas that are also producing cane sugar. And employees are paid at a rate which is well in excess of the minimum wage. So that the people who work in the production of sugar and pineapple receive a wage which exceeds the minimum wage, and that produces in and of itself a higher production cost.

The companies have intensified their ability to produce at a given volume per acre however, and as a result, we are competitive with domestic production of sugar in the United States. But the minute you have the dumping and the below-cost-of-production sales coming from other areas, then we can't compete.

Chairman GIBBONS. Since the land is not suited to alternatives to sugar, sugar is the only thing you can grow on it, the only thing you can use it for is sugar, why does the price continue to go up?

Mr. HEFTEL. The value of the land increases because if you stop producing sugar, parts of that total area that are in sugar production would go into development.

Chairman GIBBONS. That is the same problem we have in Florida.

Mr. HEFTEL. But you wouldn't have, you know, all of the land in the sense that the economic activity is an offset against the loss in jobs. It doesn't work that way. It is only a small percentage of the total amount of land that you take out of production that would go into development and create additional economic activity.

Chairman GIBBONS. Yes.

Mr. HEFTEL. But it is the same thing that you are describing to a lesser degree.

Chairman GIBBONS. Well, I am certainly in deep sympathy with the problem. Anthurium, that is the flower that has a red whatever it is that sticks out from it.

Mr. HEFTEL. Yes.

Chairman GIBBONS. Boy, they sure mark up the price when they get here, don't they? From 20 cents—they are very expensive flowers.

Mr. HEFTEL. The wholesaler to the retailer on the mainland maintains a pretty good profit margin. We won't get into that today, though.

Chairman GIBBONS. Well, I appreciate your coming and informing us of the problems that Hawaii has there.

Mr. Bailey.

Mr. BAILEY. I would like to thank the gentleman. I share many of your fears and I think that when you look at any trade initiative or any trade change, it has to be looked upon in balance. You have to look at it in terms of underlying principles and what we are trying to accomplish. It may be a mere transfer of income, for example, to the Caribbean Basin without truly providing some of the transfers of some of the benefits of this system that you have mentioned.

We have been able to maintain a relatively even distribution of wealth; we have a very large middle class. Given world economies, our society is a pretty stable one, obviously a free and open one. A system doesn't operate fairly when you simply take a small segment, because perhaps they are not politically strong or numerous, and say well, you pay the price, you are the sacrificial lamb. That is just not fair. There is no equity in that.

By the same token, I think it can be said of our country that, you know, we have maintained in relative terms, a reasonably free and open market access here, but you have got a lot of Americans out there that are starting to say, you know, geez, why am I paying the price of these transfers. Somebody wants to get a small jump on utilizing market access here, and how many benefits are you really going to confer or transfer to those people down there. I don't know about that. I don't know if this thing is structured properly in that way. We have the same problem I think with Puerto Rico and the Virgin Islands. It sounds as if you have got a very reasonable wage base rate in Hawaii. I am sure given your cost of living and everything, that certainly doesn't sound excessive to me. At least I have never viewed it as excessive.

Mr. **Heftel**. The employees don't think it is excessive.

Mr. **Bailey**. No, I am sure that they don't. But the point is I have never heard it described as really excessive or abusive. Now, you know, people make those arguments on industrial wage rates in this country and modernization is affected by them and that sort of thing, but I don't really share those views. That doesn't make me right or wrong, but that is my view. In this case, I couldn't agree with you more. I think that we have an obligation to look at both sides of the coin, or you can't go to that American taxpayer and say that you can justify this kind of policy.

The other thing is the long term distortion. What do you do when you wake up in 10, 15, 20 years and you have conferred a certain amount of employment. I doubt very much if we are going to accomplish that much with this program the way it is envisioned. And somebody else screams for a change or somebody else argues about what you are doing with your international trade policy, and this is a distortion also. So I recognize the problem, I think the way you do, and we have got to do something with it. I hope we can be more imaginative and more respectful of the American needs that are involved.

So I agree strongly with the gentleman's concerns and appreciate very much the very reasonable approach taken to it. Our chairman has done the same thing, and I agree with his views on it. We have to look at this thing in context, and in balance, and be concerned about some of those displacements.

I thank you very much.

Mr. **Vander Jagt**. Mr. Chairman, I would just like to thank our distinguished colleague, a colleague not only in the Congress but on the Ways and Means Committee, for being here.

Mr. **Heftel**. Thank you very much. Thank you very much, Mr. Chairman.

[The prepared statement follows:]

STATEMENT OF HON. CECIL (CEC) HEFTEL, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF HAWAII

Mr. Chairman: I appreciate this opportunity to appear before you this morning to discuss the Administration's proposed Caribbean Basin Initiative. I have followed very closely the development of the Caribbean Basin Economic Recovery Act and, while I applaud the Administration's focus on economic aid to this region, I nevertheless must say that as a representative from Hawaii I am greatly concerned about the free trade component of this proposal.

Specifically, I am concerned about any proposals which encourage an increase in sugar and other agricultural imports, including pineapple and papaya, from the Caribbean. Our domestic sugar industry already faces strong competition from Caribbean Basin countries. With additional trade incentives such competition could prove devastating to a presently endangered industry. Indeed, the Caribbean currently accounts for well over ten percent of our sugar imports. We must be careful in our efforts to promote economic growth in this region that we do not inadvertently overwhelm hard-pressed domestic industries.

I have referred to the sugar industry in Hawaii as an endangered industry. Let me elaborate. Although Hawaii's sugar industry is notedly efficient, it nevertheless suffered an estimated $83 million in losses last year. These losses were caused by competition with subsidized foreign sugar, sugar which is openly "dumped", if you will, on our domestic market. Losses are likely to be another $80 million this year. The impact of these losses, both realized and anticipated, is reverberating in my state.

One of our leading companies has announced plans to permanently close a plantation employing more than 550 workers. This action will take more than 16,000 acres out of production. This is land, I should add, which is difficult to convert to other agricultural crops. Many Hawaii sugar workers have already agreed to postpone scheduled wage increases—others may very well follow suit. Let me emphasize that we are talking about an industry in my state which employs 9,000 people directly and indirectly supports the jobs of another 21,000 workers.

I do appreciate the fact that the Administration plan calls for an absolute limit of 1.15 million metric tons of sugar entering the United States from the largest Basin suppliers: the Dominican Republic, Guatemala, and Panama. However, this quota would still permit an approximate 10 percent increase in the average exports from these countries to the United States. Sugar from the smaller Basin suppliers, as I understand it, would continue to enter under the Generalized System of Preferences, subject to GSP limits. All sugar entering from the Caribbean Basin countries would continue to be subject to the Section 22 fee which may very well have to be raised. I should point out that these steps are being proposed as a direct result of the sugar price support program contained in the Farm Bill passed by Congress last year. Regardless of these sincere efforts to limit imports, however, it is clear that the Caribbean plan places additional pressures on an already overburdened industry. Needless to say, it is imperative that the provisions of this proposal are structured so that they do not in any way jeopardize the Farm Act's sugar support program.

Let me shift the focus of my concern for a moment to another Hawaii commodity—pineapple. As a result of foreign competition in the early 1970's, serious market disruptions were caused for Hawaii pineapple growers. We found that we could simply not compete with the low labor costs enjoyed by foreign growers. As a result, three of Hawaii's four pineapple companies in 1973 undertook major cutbacks and closures. Today, pineapple acreage in Hawaii is approximately two-thirds the amount it was in 1972. Since 1972, pineapple imports to the United States have increased 186 percent. It was announced earlier this year that Dole's pineapple cannery in Honolulu, one of the world's largest, would close for three months. Low cost foreign competition flooding the market was blamed. Two hundred eight permanent employees and 450 intermittent workers were affected by the action.

The fresh papaya and sweet ginger industries are good examples of fledgling concerns which are threatened by imports. A sudden increase in papaya and ginger imports could undo long years of patient efforts by our domestic producers, who have been carefully expanding their markets through high quality control and aggressive promotion. Hawaii, for all practical purposes, is the only state in which pineapple, papaya, and sweet ginger are produced and marketed. It is clear that Hawaii would certainly bear the brunt of the impact of increased duty-free imports of these products.

I met just this week with a representative of the Hawaii floral industry. I was advised that Hawaii growers sell anthuriums, a tropical flower, for twenty cents each. This price includes the cost of growing, processing, and transporting the flower to the continental U.S. market. Jamaica, which has a similar climate and growing conditions, also produces anthuriums. Growers there are selling the same flower in the same U.S. market for three cents each. This type of price-cutting makes it virtually impossible for growers in Hawaii to even try to compete. How can we hope to establish and maintain a domestic industry under these conditions? The answer is that it cannot be done.

Mr. Chairman, let me conclude by pointing out that Hawaii does not enjoy a diversified economy as many of the mainland states do. Our transportation considerations, high labor costs, relative isolation, and other factors contribute to the unique situation in which we find ourselves. Hawaii's uniqueness as a state should certainly be taken into account as the Caribbean Basin Initiative is scrutinized by Congress. At the same time, I am concerned that we do not yet know the full import of this proposal, particularly its economic impact on Hawaii and the nation as a whole. Until the impact of the legislation before us is more fully understood, I must urge that a most cautious approach be taken.

I am confident that my colleagues on the Trade Subcommittee will evaluate this proposal most carefully, Thank you for giving me this opportunity to share with you and the members of your committee my views on an issue of critical importance to the people of Hawaii.

Chairman GIBBONS. Thank you.

Our next witnesses are a group of individuals from the Council of the Americas. Mr. Wolfe, maybe you are the only one. I wasn't reading far enough ahead.

Mr. WOLFE. Mr. Chairman, I am all alone.

Chairman GIBBONS. Go right ahead, Mr. Wolfe.

STATEMENT OF ALEXANDER WOLFE, JR., VICE CHAIRMAN, COUNCIL OF THE AMERICAS

Mr. WOLFE. Mr. Chairman, my name is Alexander Wolfe. I am president of Southeast Bank in Florida and vice chairman of the Board of the Council of the Americas. I think you know the Council of the Americas is a nonprofit organization of more than 200 U.S. companies and they do comprise a substantial portion of the private investments in Latin America and the Caribbean. It is on behalf of that association, the council, that I am very pleased to have this opportunity to testify in support of the administration's Caribbean Basin Economic Recovery Act.

Today the Caribbean Basin is a patchwork of troubled and fragile economies. High unemployment, spiraling inflation, rising energy prices, declining tourism and decreasing commodity prices have all combined to create an environment of economic and, indeed, political instability. Political unrest in some of the countries of the region has quickly followed these economic difficulties, and the effects on our country are becoming more pronounced every day as refugees from this Caribbean Basin pour in. Many come in search of desperately needed jobs, others to escape political violence. It is an unending tragedy.

Meanwhile, this country's already hard-pressed taxpayers are having to shoulder the increasing day-to-day costs of providing for the displaced individuals. Communities such as mine, Miami, literally have reached the saturation point. That is why this program has particular relevance to me, in addition to my testimony for the Council of the Americas, not only as a businessman—and we do conduct business in the Caribbean—but also as a resident of a community that has experienced firsthand the destructiveness the region's failing economies have had, as well as its political crises, on all of our personal lives.

President Reagan, in introducing this legislative package to Congress, referred to it as a different kind of program, one designed to "improve the lives of the peoples of the Caribbean Basin by enabling them to earn their own way to a better future." This is, indeed, a departure from past policies. Traditionally, aid has been channeled almost exclusively through the public sector. The current proposal reflects a recognition that the productive capacity of the private sector, and its potential for self-sustaining growth, needs to be engaged in new ways. By blending and reinforcing trade, investment, and aid measures, the administration's program strikes at the very heart of the problem. It creates a positive balance between public and private sector development efforts. Both sectors have important roles to play in the development process, and can jointly maximize their impacts under this flexible program.

I would like to emphasize, however, that these efforts represent only a first step in what must be a coordinated process, a process that must include diplomatic efforts to bring peace in the area.

It would be a mistake to assume that large multinational companies are going to provide the magic cure to the region's economic ills.

Given the area's relatively modest market size, it is the small- and medium-size businesses, particularly local, but including foreign, which most appropriately can and should play the dominant role.

Let me focus more specifically on how I think the program will affect that role. Insuring long-term economic stability will hinge largely on developing the self-sustaining productive capacity of the local private sector. This legislation does that by opening new markets here, providing at the same time, through foreign investment, the transfer of technology and know-how that will allow local entrepreneurs to take advantage of this expanded opportunity, and by making available credit to fund necessary production capacity.

Certainly we all recognize that certain American industries and unions may be concerned about large increases in imports of low-cost, duty-free items from the Caribbean Basin if this proposal is enacted. We do not believe that there are going to be any sudden, major increases in these imports. Whatever the U.S. tariff treatment, neither American nor foreign investors are going to rush to put up new facilities in the Caribbean Basin, for the political reasons I have already mentioned.

Then why enact the one-way free trade treatment? It should be enacted to permit gradual increases in private investment as stability increases in the region, and because it will provide encouragement to the private sector there at a time when it badly needs encouraging.

As strong as this program is, however, we believe it could be further strengthened in the area of tax concessions. An alternative that we believe would yield an even more positive impact would be a targeted tax sparing. Under tax sparing, the United States would not collect the tax spared by a Caribbean country when it extends a tax holiday in an effort to attract investment. Sparing can be targeted at employment generating indigenous activities which can only take place in the Caribbean, thereby avoiding any loss of U.S. jobs. Sparing also involves no revenue loss to the U.S. Treasury.

Almost all of our developed country competitors provide tax sparing, and the less-developed countries have been requesting it for years. Let me give you an example of how targeted tax sparing would work. Currently, if Jamaica, for example, reduces its corporate income tax by 20 percent to stimulate job creation and investment, American business—because it is paying a lower tax in Jamaica—will have its U.S. tax credits reduced by an equal amount and will thus pay a higher tax here. Not only does this prevent any benefits from accruing to the U.S. business, it also obviously eliminates any incentive on the part of the Caribbean nations to use tax policy to stimulate local employment where the U.S. investor is concerned.

Under targeted tax sparing, the U.S. Treasury would receive precisely the same amount of revenue that it would have received had Jamaica not further reduced its taxes to stimulate investment, leaving the additional cash flow available to be reinvested in job-creating enterprises.

Such measures, coupled with the free trade area concept and direct assistance package, give this program a balance that offers the prospect of a continuing partnership between the private and public sectors in the development process. It also allows us to share the burden of development with our more developed neighbors and, most important of all, it puts the emphasis on the local private businessman, the only actor in this play who can guarantee long-term self-sustaining growth. It is upon that prospective growth that the well-being of the peoples of the Caribbean depends. Without it, economies will continue to weaken, political violence will spread, and lives will continue to be ruined as individuals are forced to flee their homes. In no recent time has the choice been clearer. By helping our neighbors we can help ourselves.

Mr. Chairman, if I might give you a little idea of the consequence of the refugee problem, the State of Florida estimates that since the Muriel boat lift in the spring of 1980, the costs in Florida for providing for Cuban nation refugees have come to an estimated $368 million. Granted that Muriel thing was a special case, but clearly the potential for new influx exists. Some relief agencies estimate that upward of 500,000 Salvadorans of a population of 5 million have fled their country's violence and come into the United States. According to some estimates in Miami, 200 Haitians are still entering Florida every week. These, of course, are rough estimates. But when we talk about employment and burdens on our taxpayers, I think that should be borne in mind.

Thank you, Mr. Chairman.

[The prepared statement follows:]

STATEMENT OF ALEXANDER WOLFE, JR., VICE CHAIRMAN, COUNCIL OF THE AMERICAS

Mr. Chairman:

My name is Alexander Wolfe, Jr., and I am President of Southeast Bank, N.A. I am also a vice chairman of the Board of the Council of the Americas, a non-profit association of more than 200 U.S. companies comprising a substantial majority of private investments in Latin America and the Caribbean. It is on behalf of the Council that I am pleased to have this opportunity to testify in support of the Administration's Caribbean Basin Economic Recovery Act.

The Caribbean Basin today is a patchwork of troubled and fragile economies. High unemployment, spiraling inflation, rising energy prices, declining tourism and decreasing commodity prices have combined to create an environment of economic instability. Political unrest in some countries of the region has quickly followed, and the effects on our country are becoming more pronounced every day as refugees from the area continue to pour in. Many come in search of desperately needed jobs, others to escape political violence. It is an unending tragedy.

Meanwhile, this country's already hard-pressed taxpayers are having to shoulder the increasing day-to-day costs of providing for the displaced. Communities such as Miami literally have reached the saturation point. That is why this program has particular relevence to me, not only as a businessman who conducts business in the Caribbean, but also as a resident of a community that has experienced firsthand the destructiveness the region's failing economies as well as its political crises, have had on personal lives.

President Reagan, in introducing this legislative package to Congress, referred to it as a different kind of program, one designed to "improve the lives of the peoples of the Caribbean Basin by enabling them to earn their own way to a better future." This is, indeed, a departure from past policies. Traditionally, aid has been channeled almost exclusively through the public sector. The current proposal reflects a recognition that the productive capacity of the private sector, and its potential for self-sustaining growth, needs to be engaged in new ways. By blending and reinforcing trade, investment, and aid measures, the Administration's program strikes a positive balance between public and private sector development efforts. Both sectors have important roles to play in the development process, and can jointly maximize their impacts under this flexible program.

Another unique aspect of this proposal is the coordinated multinational effort that also includes Canada, Mexico, and Venezuela, working together to provide the peoples of the region with the means to help themselves. We, therefore, certainly are not being left to shoulder this burden alone as has at times been the case in the past.

I would like to emphasize, however, that these efforts represent only a first step in what must be a coordinated process -- a process that must include diplomatic efforts to bring peace to the area. For although this package will go a long way toward creating a more positive investment climate, it in no way can realistically be expected to succeed in a country being wracked by violent upheaval. Investors, local and foreign, simply are not going to invest in areas embroiled in armed conflict, no matter what the incentives.

It would be a mistake to assume large multinational companies are going to provide the magic cure for the region's economic ills. Given the area's relatively modest market size, it is the small and medium size businesses, particularly local, but including foreign, which most appropriately can and should play the dominant role.

Let me focus more specifically on how we think the program will affect that role. Insuring long-term economic stability will hinge largely on developing the self-sustaining productive capacity of the local private sector. This legislation does that by opening new markets here, providing at the same time, through foreign investment, the transfer of technology and know-how that will allow local entrepeneurs to take advantage of this expanded opportunity, and by making available credit to fund necessary production capacity.

Specifically, the program expands markets for local private business by one-way free trade treatment to the countries in the region for 12 years. Although textiles and apparels would be excluded, the Administration plans to extend more favorable treatment to the region under our overall textile policy. We strongly hope that the Administration and the Congress will resist pressures to exclude additional products or industries from the one-way free trade treatment. In fact, our preference would be to grant this treatment to types of hand-made apparels which are not made here.

Under a second major provision, a ten percent investment tax credit, operating under the same guidelines as the current domestic investment credit now in place, would be extended to new investments in the Caribbean.

Finally, a $350 million Fiscal Year 1982 supplemental aid package will provide fast-acting balance of payments support. Fiscal Year 1983 development monies will be used to provide managerial and technical training.

We recognize that certain American industries and unions may be concerned about large increases in imports from low-cost, duty-free items from the Caribbean if the Administration proposal is enacted. We do not believe that there are going to be any sudden, major increases in these imports. Whatever the U.S. tariff treatment, neither American or foreign investors are going to rush to put up new facilities in the Caribbean Basin, for reasons to which I have already alluded.

Then why enact the one-way free trade treatment? It should be enacted to permit gradual increases in private investment as stability increases in the region, and because it will provide encouragement to the private sector there at a time when it badly needs encouraging.

We are optimistic about this program. Coupled with executive actions that will include the negotiation of bilateral investment treaties, expansion of U.S. Export-Import Bank lending, and development of additional insurance facilities, we think this package will yield the desired results.

As strong as this program is, however, we believe it could be further strengthened in the area tax concessions. The ten percent investment credit in of itself is a positive provision, and should very definitely remain a part of the package if Congress decides not to approve an alternative tax measure. But an alternative that we believe would yield an even more positive impact would be targeted tax sparing. Under tax sparing, the United States would not collect the tax "spared" by a Caribbean country when it extends a tax holiday in an effort to attract investment. Sparing can be targeted at employment generating indigenous activities which can only take place in the Caribbean, thereby avoiding any loss of U.S. jobs. Sparing also involves no revenue loss to the U.S. Treasury.

Almost all of our developed country competitors provide tax sparing, and the less-developed countries have been requesting it for years. Targeted tax sparing will make the U.S. private sector more competitive in the Caribbean in relation to industry from these developed countries who, because of tax sparing, can capture the tax flow from local incentive programs for reinvestment and job creation.

Let me give an example of how targeted tax sparing would work. Currently, if Jamaica, for example, reduces its corporate income taxes by

20 percent to stimulate job creation and investment, American business -- because it is paying a lower tax in Jamaica -- will have its U.S. tax credits reduced by an equal amount and will thus pay a higher tax here. Not only does this prevent any benefits from accruing to the U.S. business, it also obviously eliminates any incentive on the part of Caribbean nations to use tax policy to stimulate local employment where the U.S. investor is involved.

Under targeted tax sparing, the U.S. Treasury would receive precisely the same amount of revenue that it would have received had Jamaica not further reduced its taxes to stimulate investment, leaving the additional cash flow available to be reinvested into job creating enterprises.

Such tax measures, coupled with the free trade area concept and direct assistance package give this program a balance that offers the prospect of a continuing partnership between the private and public sectors in the development process. It also allows us to share the burden of development with our more developed neighbors. And most important of all, it puts the emphasis on the local private businessman, the only actor in this play who can guarantee long-term self-sustaining growth. It is upon that prospective growth that the well-being of the peoples of the Caribbean depends. Without it, economies will continue to weaken, political violence will spread, and lives will continue to be ruined as individuals are forced to flee their homes. In no recent time has the choice been clearer. By helping our neighbors we can help ourselves. This program provides us the way.

Thank you.

Chairman **Gibbons**. Thank you. Mr. Bailey has a conflict, so we will allow him to go first.

Mr. **Bailey**. Thank you very much, Mr. Chairman. I have just a couple of remarks. I have a subcommittee downstairs I have to get to. They are dealing with unemployment compensation for ex-service members, which is an issue I have been working on.

I just wanted to tell you that in my mind this is the best statement I have seen prepared and delivered in terms of concepts, at the very least, before the subcommittee, and I agree with the view that you are taking implicitly. I think it is very balanced. It recognizes the realities that we have got to do something in the interest of world political stability, in the interest of the economic system, the political system in which we believe. It also faces the reality that the problems just flat aren't simple and that we have got to deal with structural unemployment problems in this country in order to justify to American taxpayers the kind of changes we want to make, because we have put a lot of effort into building up this economy and this political system, and that has to be recognized. I think it is just—the general recommendations I think are excellent. I really applaud you for them.

I hope I can get to know you folks better and receive the benefit of your advice in the future. I really think it is a balanced overall view, and I think if we had approached this thing from this standpoint earlier we would be a lot better off.

I noticed in your statement here, second paragraph on page 3, "even if an industry could make a good case for Government help under the current escape clause," going on. One of the most discouraging things for me is an indication on the part of the administration apparently not to want to put this policy out there where it can be discussed, or its ramifications or impact on people can be discussed. We had testimony to that effect from the ITC and it was a specific decision made. I am going to ask the members of the subcommittee and the chairman to make sure that that change is one that we incorporate, that the Congress is advised and we are advised of the impact of this policy should they succeed with it.

Again, I have to leave, but thank you. I really appreciate it.

Mr. **Wolfe**. Thank you.

Mr. **Bailey**. Thank you, Mr. Chairman.

Chairman **Gibbons**. Yes, sir, Mr. Bailey.

Mr. Wolfe, I appreciate your coming. I know full well the problems the community of Miami and the Dade County area have had with the influx of aliens.

You make an interesting suggestion about tax sparing, and I will have to admit that I have had little experience with this as a concept. Could you elaborate a little more on what you mean by tax sparing, and perhaps even tell us what areas you think it ought to be used in.

Mr. **Wolfe**. I think when we are talking taxation benefits, we are not talking tax benefits to those who are mounting General Motors plants in countries. That could be investment tax credits and other types of credits. This program really isn't designed for massive factories or massive investments where a tax advantage for investment comes in. I think we are trying to create tax advantages that create employment and the economic well-being of people. So tax sparing, in our opinion, rifles directly in on that and targets it. It targets in to the degree that it would eliminate that advantage for products that are directly competitive with things manufactured in this country. It would be focused on things that are indigenous to the Caribbean. It is a targeted approach which in the long run, in our opinion, is of more benefit to indigenous companies than any other form of offset we could put into effect, and it is less costly to the Government. So it is I think to us the clear-cut way to go. Perhaps there is a better idea.

Chairman GIBBONS. How would it work in practice?

Mr. WOLFE. I think the Jamaica case I raised is typical. If you invest and Prime Minister Seaga reduces taxes down there and that reduction is offset by increased taxes up here, the net is zero. If we had tax sparing, that is a net benefit to any American investor going in there. Small investors are spared U.S. tax, on that Jamaican tax reduction. He continues to pay the tax he paid before, but his full tax benefit comes through, and that is of interest, unless he is building a large plant. But we don't visualize very large industries going into the basin.

Chairman GIBBONS. Of course in the Jamaica illustration you give there, the hotel would have to be American-owned and it would have to——

Mr. WOLFE. Have to have American investment.

Chairman GIBBONS. It would have to have American investment. And what other kinds of businesses could be developed in that area that would not be competitive with someplace, Florida, Hawaii as we have heard, Puerto Rico?

Mr. WOLFE. Well, it is hard to say except if you stated something to do with the coffee, it is clear you can't produce coffee in Kalamazoo. So indigenous products, there are many in the Caribbean Basin. But we really feel it is targeted so that it wouldn't cause upsets in our market and create free off-shore zones which don't really help the local people. Based on indigenous types of work. Maybe another example would be do we really produce up here West Indian textiles which are not textiles; they are a very different kind of material created in the West Indies. That doesn't compete with anything up here. There are a multitude of things in these small islands that they can do and do well that don't have direct competition with our own industry up here.

Chairman GIBBONS. Mr. Vander Jagt?

Mr. VANDER JAGT. I would like to thank the witness for a very excellent statement.

Mr. WOLFE. Thank you, sir.

Chairman GIBBONS. Mr. Frenzel?

Mr. FRENZEL. No questions.

Chairman GIBBONS. Thank you very much.

Mr. WOLFE. Mr. Chairman, thank you.

Chairman GIBBONS. Yes, sir.

Our next witness is Mr. Steve Koplan of the American Federation of Labor and the CIO.

Mr. Koplan, we welcome you. You are certainly no stranger to this committee. We are glad to have both of you here today, and will be pleased to listen to you.

Mr. KOPLAN. Thank you, Mr. Chairman. With me is Elizabeth Jager, as you know, trade economist in our department of economic research.

Mr. Chairman, I will not read my entire statement, but I would ask that the statement be included in its entirety.

Chairman GIBBONS. Certainly, it will be.

STATEMENT OF STEPHEN KOPLAN, LEGISLATIVE REPRESENTATIVE, DEPARTMENT OF LEGISLATION, AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS, ACCOMPANIED BY ELIZABETH JAGER, ECONOMIST

Mr. KOPLAN. Thank you.

The AFL-CIO appreciates this opportunity to present our views on the Reagan administration's Caribbean Basin Economic Recovery Act, H.R. 5900.

AFL-CIO union members look upon those who live and work in the Caribbean Basin as their brothers and sisters—in many cases this is literally the relationship. In addition, thousands of U.S. union members live and work in Puerto Rico and U.S. insular possessions in the region. All of these workers know the problems of runaway factories from the mainland and among the islands. Wage exploitation and massive unemployment that can develop from mismanaged policies are not new to them. Neither the workers in the Caribbean nor the workers in the United States want programs that cost one another jobs and thus lead to more unemployment.

The AFL-CIO does support direct economic assistance in the form of a supplemental appropriation for the countries in this region desperately in need of help. We do urge that the $350 million sum provided in H.R. 5900 be carefully scrutinized to determine whether that amount is appropriate for fiscal year 1982.

However, the AFL-CIO is strongly opposed to the trade and tax incentives contained in the bill. Those incentives will only serve to further weaken the U.S. industrial base by encouraging new runaways by U.S. industries to the Caribbean region, result in a quickening of lost U.S. jobs—skilled as well as unskilled—and create windfall benefits for non-Caribbean countries from the Soviet Union to the Far East.

Title I of the bill lists 28 countries in the Caribbean Basin as potentially eligible "beneficiary countries" for so-called one-way free trade with the United States—zero tariffs on U.S. imports from those countries designated for 12 years.

Let me just stop for a moment, Mr. Chairman, and say it is our understanding that other countries are participating in this project on a coordinated basis—Canada, Mexico, and Venezuela. But I point out that none of those countries are engaging in the kind of one-way free-trade and tax program that is being proposed in H.R. 5900. We stand alone in that regard.

However, the administration admits that at present about 87 percent of the products of those countries, referring to the Caribbean region, already enter the United States duty-free under the Generalized System of Preferences for less developed countries. Its reason for blithely requesting absolute authority to "grant duty-free access for all Caribbean Basin imports with the exception of textiles and apparel covered by textile agreements," is mind-boggling.

To quote Ambassador William Brock's statement before this subcommittee on March 17, it is because "there is uncertainty and fear in the Caribbean Basin about the future of the GSP program." On that same day, the General Counsel for the Office of the U.S. Trade Representative, Donald de Kieffer, testified in the Senate that "many potential Caribbean exports have never been included in this scheme," referring to GSP. "Other products have been eliminated from eligibility through the GSP petition process or by the competitive need limitations." For those reasons, according to Mr. de Kieffer, the trade provisions of the Caribbean Basin Initiative were crafted.

Mr. Chairman, why does the administration choose to abolish the modest existing congressional limitations for GSP benefits? Why does it instead expand those benefits massively beyond the 2,900 imported products now entering the United States duty-free under GSP, rather than deal directly with the future of the GSP program scheduled to end in 1984? The approach taken in H.R. 5900 makes a mockery of congressional intent in 1974 when GSP was enacted.

The AFL-CIO opposed GSP in the Trade Act of 1974. But with all of its shortcomings, that law at least tailored GSP somewhat in an attempt to limit the damage. I give illustrations of that in my testimony. H.R. 5900 would sweep away these protectives, minimal as they are.

If H.R. 5900 is adopted, massive trade diversions—a flood of imports worldwide—can be funneled through any one or any combination of these 28 Caribbean Basin countries. Imports of virtually any product made anywhere in the world will also be able to penetrate the U.S. market through the U.S. Virgin Islands, Guam, and American Samoa. All that will be necessary is the claim that 25-percent local content of the product originated in the Caribbean Basin region, or in U.S. insular possessions—even GSP requires a higher local content requirement of 35 percent. If the contributions are combined from two or more countries, then under GSP the minimum material or processing value is raised from 35 percent to 50 percent.

The ridiculously low local content provisions in H.R. 5900 make all industries in the United States subject to assaults from imports—without benefiting the economies of the Caribbean. Internal market growth with rising living standards—not trade diversions—should be the route to economic development. If trade is to be used to help build healthy industries within the Caribbean countries, the bill should have much higher content provisions.

Past experience has taught us that assembly and pass-through arrangements, like those contained in the bill, can be used to sidestep U.S. trade and tariff laws and in that regard, we give an example of Soviet watches.

Mr. Chairman, the trade provisions of the bill contain no effective safeguards for U.S. industries against injury from imports. The bill empowers the President to designate any country as a beneficiary country if he "determines that such designation will be in the national economic or security interest of the United States and reports such determination to the Congress with his reasons therefor." Moreover, if injury is claimed by a U.S. industry, it is no longer sufficient for the International Trade Commission to make a determination under the 1974 Trade Act that an article is being imported into the United States in such increased quantities as to be a substantial cause of serious injury. The bill imposes a new unrealistic burden on the ITC—to determine that the injury results from the duty-free treatment afforded under the Caribbean Basin Initiative.

Mr. Chairman, the third-quarter of 1981 showed a sharp rise in U.S. imports not only of apparel but also of tires, glass, hand tools, nuts and bolts, machine tools, roller bearings, semiconductors, motor vehicle parts, canned fish, aircraft engines, and spacecraft parts. Are American workers now to be sent a legislative message that for the next 12 years, U.S. trade policy will encourage a continuous loss of U.S. jobs in each of these products or parts of products as well as the more sophisticated manufactures that we were told would comprise this country's new industrial base? It is mystifying that the administration's trade incentives for the CBI are proposed at a time when our Nation already has a trade deficit of $40 billion with the world that includes a $3.2 billion deficit with the Caribbean Basin countries. At the same time, the U.S. value of imports receiving GSP treatment has risen to $8.4 billion, up from $3 billion just 6 years ago.

In sum, the administration's trade incentives are ill-conceived and unthinkable when balanced against the misery brought by nearly 9-percent U.S. unemployment. Such incentives for further increases in unemployment must be rejected.

The tax incentives proposed in title III are equally astounding. Just last year, the administration sold the Congress on a package of business-tax incentives that will result in hundreds of billions of lost revenues to the Treasury. This was done ostensibly to encourage increased investment and productivity in the United States. Pictures were painted of countless purchases of machinery and equipment, plants springing up all over our Nation, and of course shrinking unemployment lines. Now in title III of H.R. 5900, the administration is proposing "an unprecedented extension for 5 years of the investment tax credit to property which is used predominantly in certain Caribbean Basin countries and which would otherwise qualify for the domestic investment tax credit." The purpose of this proposal is admittedly to "encourage the placement of machinery and equipment in the Caribbean Basin."

Not only will the credit be allowed to a U.S. citizen, resident or corporation investing in such property, but the credit would also be passed through a U.S. shareholder who owns 5 percent or more in value of the outstanding stock of a foreign corporation. The purpose of this provision is to encourage new equity investment in the basin that is permanent in nature. According to the administration, its investment tax credit proposal will cost the Treasury about $50 million in 1983 and a total of nearly $300 million during the 5 year period of the extension.

In addition, the administration proposes extending the newly enacted accelerated cost recovery system and the investment tax credit to U.S. corporations operating in Puerto Rico and the U.S. insular possessions. It is ironic that the cost of this provision to the

Treasury would have paid for the $100 million in trade adjustment assistance training moneys originally supported by the administration but in its judgment no longer affordable. Yet the purpose of this provision is to further the flight of business from the United States.

The total tax incentives in the bill amount to over $800 million, but that does not represent their real cost. First, admittedly, the estimates don't take into account behavioral change that will result if this law is enacted. Second, when coupled with the bill's so-called trade incentives, the real cost will be higher U.S. unemployment caused by the manipulation of these proposals by the shippers who funnel worldwide U.S. imports through the Caribbean region. This will be accompanied by diminished U.S. investment in our own domestic industries and further decreases in U.S. industries' productivity. The trade and tax incentives will not answer the problems that must be addressed to develop Caribbean nations. They will simply assure continued swollen profits for multinationals at the expense of the U.S. economy.

Mr. Chairman, there must be a more intelligent and meaningful way to address the very real problems of the Caribbean Basin than what is proposed in H.R. 5900. This is simply a legislative package that trumpets to the world and to U.S. industry that this Nation is not interested in preserving its industrial base, that it is not interested in preserving or creating jobs in industry, services, and business here, but is bent on offering sufficient added incentives for businesses to abandon this country and its citizens. The AFL-CIO urges that the subcommittee send the administration back to the drawing board to design a more thoughtful plan of assistance to that area—not a blueprint to further pauperize America. At the least, that plan should include recognition of the past effects of runaway industries in the Caribbean countries and the current plight of the U.S. economy.

I thank you, Mr. Chairman.

[The prepared statement follows:]

STATEMENT OF STEPHEN KOPLAN, LEGISLATIVE REPRESENTATIVE, DEPARTMENT OF LEGISLATION, AFL-CIO

(1) The AFL-CIO does support direct economic assistance in the form of a supplemental appropriation for the countries in the Caribbean Basin desperately in need of help. We do urge that the $350 million sum provided in H.R. 5900 be carefully scrutinized to determine whether that amount is appropriate for fiscal year 1982.

(2) The AFL-CIO is strongly opposed to the trade and tax incentives contained in the bill. Those incentives will only serve to further weaken the U.S. industrial base by encouraging new runaways by U.S. industries to the Caribbean region, result in a quickening of lost U.S. jobs—skilled as well as unskilled—and create windfall benefits for non-Caribbean countries from the Soviet Union to the Far East.

(3) If H.R. 5900 is adopted, massive trade diversions—from a flood of imports worldwide—can be funneled through any one or any combination of 28 Caribbean countries by satisfying a ridiculously low local content requirement of 25 percent for the Caribbean region or U.S. insular possessions.

(4) The trade provisions of the bill contain no effective safeguards for U.S. industries against injury from imports. They are ill-conceived and unthinkable when balanced against the miseries brought by nearly 9 percent U.S. unemployment.

(5) The total tax incentives in the bill amount to over $800 million but that does not represent their real cost. The real cost will come from diminished U.S. investment in our own domestic industries and further decreases in U.S. industries' productivity. Additionally, the tax incentives will simply assure continued swollen profits for multinationals at the expense of the U.S. economy.

(6) The AFL–CIO believes there must be a more intelligent and meaningful way to address the very real problems of the Caribbean Basin than the tax and trade provisions proposed in H.R. 5900.

STATEMENT

The AFL–CIO appreciates this opportunity to present our views on the Reagan Administration's "Caribbean Basin Economic Recovery Act," H.R. 5900.

At its meeting in Bal Harbour, Florida, the AFL–CIO Executive Council made the following statement dated February 15, 1982, regarding the Administration's proposal: "aid in the development of Caribbean nations needs to be enhanced, but proposals for "one-way" free trade and additional investment incentives to U.S. firms for investing abroad should be rejected." (Full text of statement attached)

AFL–CIO union members look upon those who live and work in the Caribbean Basin as their brothers and sisters—in many cases this is literally the relationship. In addition, thousands of U.S. union members live and work in Puerto Rico and U.S. insular possessions in the region. All of these workers know the problems of runaway factories from the mainland and among the islands. Wage exploitation and massive unemployment that can develop from mismanaged policies are not new to them. Neither the workers in the Caribbean nor the workers in the United States want programs that cost one another jobs and thus lead to more unemployment.

On March 18, 1982, the Administration's bill was introduced in both the House and Senate. Initially, let me repeat the fact that the AFL–CIO does support direct economic assistance in the form of a supplemental appropriation for the countries in this region desperately in need of help. We do urge that the $350 million sum provided in H.R. 5900 be carefully scrutinized to determine whether that amount is appropriate for fiscal year 1982.

However, the AFL–CIO is strongly opposed to the trade and tax incentives contained in the bill. Those incentives will only serve to further weaken the U.S. industrial base by encouraging new runaways by U.S. industries to the Caribbean region, result in a quickening of lost U.S. jobs—skilled as well as unskilled—and create windfall benefits for non-Caribbean countries from the Soviet Union to the Far East.

Title I of the bill lists 28 countries in the Caribbean Basin as potentially eligible "beneficiary countries" for so-called one-way free trade with the United States—zero tariffs on U.S. imports from those countries designated for 12 years. However, at present the Administration admits that about 87 percent of the products of those countires already enter the U.S. duty-free under the Generalized System of Preferences (GSP) for less developed countries. Its reason for blithely requesting absolute authority to "grant duty-free access for all Caribbean Basin imports with the exception of textiles and apparel covered by textile agreements," is mind-boggling. To quote Ambassador William Brock's statement before this Subcommittee on March 17, it is because "there is uncertainty and fear in the Caribbean Basin about the future of the GSP program." On that same day, the General Counsel for the Office of the United States Trade Representative, Donald de Kieffer, testified in the Senate that "many potential Caribbean exports have never been included in this scheme [GSP]. Other products have been eliminated from eligibility through the GSP petition process or by the competitive need limitations." For those reasons, according to Mr. de Kieffer, the trade provisions of the Caribbean Basin Initiative were crafted.

Mr. Chairman, why does the Administration choose to abolish the modest existing Congressional limitations for GSP benefits? Why does it instead expand those benefits massively beyond the 2900 imported products now entering the U.S. duty-free under GSP—rather than deal directly with the future of the GSP program scheduled to end in 1984? The approach taken in H.R. 5900 makes a mockery of Congressional intent in 1974 when GSP was enacted.

The AFL–CIO opposed GSP in the Trade Act of 1974. But with all of its shortcomings, that law at least tailored GSP somewhat in an attempt to limit the damage: by exempting some specific import-sensitive products—those products already heavily harmed by imports—and allowing for removal of others. The GSP law also contains mechanisms to limit the dollar amount and the quantity of imports that receive the preference. H.R. 5900 would sweep away these protectives, minimal as they are.

If H.R. 5900 is adopted, massive trade diversions—a flood of imports worldwide—can be funneled through any one or any combination of these 28 Caribbean Basin countries. Imports of virtually any product made anywhere in the world will also be able to penetrate the U.S. market through the U.S. Virgin Islands, Guam and American Samoa. All that will be necessary is the claim that 25 percent local content of the product originated in the Caribbean Basin region, or in U.S. insular possessions—even GSP requires a higher local content requirement of 35 percent.

The ridiculously low local content provisions in H.R. 5900 make all industries in the U.S. subject to assaults from imports—without benefitting the economies of the Caribbean. Internal market growth with rising living standards—not trade diversions—should be the route to economic development. If trade is to be used to help build healthy industries within the Caribbean countries, the bill should have much higher content provisions.

Past experience has taught us that assembly and pass-through arrangements like those contained in the bill can be used to side-step U.S. trade and tariff laws. For example, the American watch industry fought against the use of the Virgin Islands as an entry point for Soviet watches (which, it was claimed were disassembled and assembled under trade rules in the Virgin Islands) some years ago. The arrangement merely helped destroy the U.S. watch industry. Job creation in the Virgin Islands was minimal. No watch industry developed there. But importers and foreign producers benefitted.

The trade provisions of the bill contain no effective safeguards for U.S. industries against injury from imports. The bill empowers the President to designate any country as a beneficiary country if he "determines that such designation will be in the national economic or security interest of the United States and reports such determination to the Congress with his reasons therefor." Moreover, if injury is claimed by a U.S. industry, it is no longer sufficient for the International Trade Commission to determine under Section 201(b) of the Trade Act of 1974 that an article is being imported into the United States in such increased quantities as to be a substantial cause of serious injury. The bill imposes a new unrealistic burden on the ITC—to determine that the injury results from the duty-free treatment afforded under the Caribbean Basin Initiative.

Mr. Chairman, the third-quarter of 1981 showed a sharp rise in U.S. imports not only of apparel but also of tires, glass, hand tools, nuts and bolts, machine tools, roller bearings, semi-conductors, motor vehicle parts, canned fish, aircraft engines and spacecraft parts. Are American workers now to be sent a legislative message that for the next 12 years, U.S. trade policy will encourage a continuous loss of U.S. jobs in each of these products or parts of products as well as. The more sophisticated manufactures that we were told would comprise this country's new industrial base.

It is mystifying that the Administration's trade incentives for the CBI are proposed at a time when our nation already has a trade deficit of $40 billion with the world that includes a $3.2 billion deficit with the Caribbean Basin countries. At the same time, the U.S. value of imports receiving GSP treatment has risen to $8.4 billion up from $3 billion just six years ago.

In sum, the Administration's trade incentives are ill-conceived and unthinkable when balanced against the miseries brought by nearly 9 percent U.S. unemployment. Such incentives for further increases in unemployment must be rejected.

The tax incentives proposed in Title III are equally astounding. Just last year, the Administration sold the Congress on a package of business tax incentives that will result in hundreds of billions of lost revenues to the Treasury. This was done ostensibly to encourage increased investment and productivity in the United States. Pictures were painted of countless purchases of machinery and equipment, plants springing up all over our nation, and of course shrinking unemployment lines. Now in Title III of H.R. 5900, the Administration is proposing "an unprecedented extension for five years of the investment tax credit to property which is used predominantly in certain Caribbean Basin countries and which would otherwise qualify for the domestic investment tax credit." The purpose of this proposal is admittedly to "encourage the placement of machinery and equipment in the Caribbean Basin."

Not only will the credit be allowed to a U.S. citizen, resident, or corporation investing in such property but the credit would also be passed through a U.S. shareholder who owns 5 percent or more in value of the outstanding stock of a foreign corporation. The purpose of this provision is to encourage new equity investment in the Basin that is permanent in nature. According to the Administration, its investment tax credit proposal will cost the Treasury about $50 million in 1983 and a total of nearly $300 million during the 5 year period of the extension.

In addition, the Administration proposes extending the newly enacted accelerated cost recovery system (ACRS) and the investment tax credit to U.S. corporations operating in Puerto Rico and U.S. insular possessions. It is ironic that the cost of this provision to the Treasury would have paid for the $100 million in trade adjustment assistance training monies originally supported by the Administration but in its judgment no longer affordable. Yet the purpose of this provision is to further the flight of business from the U.S.

The total tax incentives in the bill amount to over $800 million but that does not represent their real cost. When coupled with the bill's so-called trade incentives, the real cost will be higher U.S. unemployment caused by the manipulation of these proposals by the shippers who funnel worldwide U.S. imports through the Caribbean region. This will be accompanied by diminished U.S. investment in our own domestic industries and further decreases in U.S. industries' productivity. The trade and tax incentives will not answer the problems that must be addressed to develop Caribbean nations. They will simply assure continued swollen profits for multinationals at the expense of the U.S. economy.

Mr. Chairman, there must be a more intelligent and meaningful way to address the very real problems of the Caribbean Basin than what is proposed in H.R. 5900. This is simply a legislative package that trumpets to the world and to U.S. industry that this nation is not interested in preserving its industrial base, that it is not interested in preserving or creating jobs in industry, services and business here, but is bent on offering sufficient added incentives for businesses to abandon this country and its citizens. The AFL-CIO urges that the Subcommittee send the Administration back to the drawing board to design a more thoughtful plan of assistance to that area—not a blueprint to further pauperize America. At the least, that plan should include recognition of the past effects of runaway industries in the Caribbean countries and the current plight of the U.S. economy.

Attachment: International Trade and Investment.

STATEMENT BY THE AFL-CIO EXECUTIVE COUNCIL ON INTERNATIONAL TRADE AND INVESTMENT

The recession-bound U.S. economy continues to lose jobs and production, a trend aggravated by mismanaged trade policies and practices. The U.S. trade balance suffered a record $40 billion deficit in 1981. As the world faces recession, many nations are increasing their barriers to imports of U.S. goods and further subsidizing their exports to the U.S. The Reagan Administration is ignoring these facts.

The Administration's monetary policies have brought a high value to the dollar—up 16 percent against major currencies since 1980—encouraging imports and retarding exports. These monetary policies have thus dealt a double blow—a downturn at home and a disaster in trade from added imports and slackening exports.

U.S. basic industries, already in need of revitalization, have been severely injured by the impact of expanded imports on top of the recession. Steel has suffered import penetration of about 20-25 percent of the U.S. market since last August. Auto imports in 1981 increased their share of a falling market to 31 percent in January. Apparel imports were over 33 percent of the market. Machinery and machinery parts imports caused new concern in a weakened market. With import pressure mounting, virtually every type of manufacturing and related services felt the brunt of lost orders both at home and abroad.

Instead of imports declining as they usually do in a recession, products of more than one-quarter of the manufacturing industries showed a sharp import rise in the third-quarter of 1981 over the same period the year before—these include such varied items as tires, glass, apparel, hand tools, nuts and bolts, machine tools, roller bearings, semiconductors, motor vehicle parts, canned fish, aircraft engines and spacecraft parts.

Even America's newest industries, the so-called "high technology industries," are beginning to be hurt by imports. By January 1982, the *New York Times* was reporting that the United States had lost its lead in computer chip technology and production of aircraft parts was expanded into closed economies—including the People's Republic of China.

While imports of manufactured goods rose 13 percent in 1981, exports of manufactured goods were up only 7 percent. There has been inadequate attention to the composition of exports. The dollar value of exports does not tell the full story in terms of jobs and products. For example, the U.S. exports much raw material involving relatively little labor instead of manufactured goods and processed foods which require considerable labor input.

Instead of continuing trade adjustment assistance promised to workers injured by imports, the Administration's 1983 budget proposal calls for a mere 1 percent of the 1981 outlays for trade adjustment assistance and a complete end of the program in 1984.

The only recognition of the need to act in the U.S. interest was the conclusion of the Multifibre Arrangement.

The AFL-CIO calls upon President and the Congress to undertake a number of specific measures in the trade area:

Placement of temporary restrictions on harmful imports during the term of the recession to prevent added penetration of U.S. markets by foreign producers and a further weakening of the U.S. industrial base.

Enactment of additional domestic content laws to protect endangered U.S. industries, such as H.R. 5133, which assures the continued U.S. capability to produce autos.

Speedy and effective handling of the dumping and subsidy cases in steel, to assure the promised redress for these unfair trade practies.

Ending of the President's continued authority to negotiate further tariff reduction.

Assurance that a portion of U.S. raw material exports be processed in this country, so that export of products such as grain, logs, etc., is conditioned upon specific domestic processing.

Establishment of bilateral shipping agreements and adherence to cargo preference laws.

Extension of the "manufacturing clause" of the U.S. Copyright Law to protect against widespread losses of jobs in the printing industry.

Extention of Trade Adjustment Assistance to provide adequate compensation to those unemployed because of trade, and improve training, job search, and relocation aid to those displaced workers who need such help.

Commitment that foreign grant, insurance and loan programs, such as the Export-Import Bank, are carefully managed to safeguard U.S. interests at home and abroad. Despite defects of the Eximbank, funds must not be slashed until other countries cut or eliminate their subsidy programs. Ex-Im Bank funds and guarantees must not be extended to any Communist countries.

Aid in the development of Caribbean nations needs to be enhanced, but proposals for "one-way" free trade and additional investment incentives to U.S. firms for investing abroad should be rejected.

Vigorous enforcement of reciprocity provisions of the Trade Act must be undertaken.

The AFL-CIO believes that enforcement of the Trade Act and the fashioning of new remedies to assure a strong and diversified U.S. industrial structure are essential for America's well being.

Chairman **Gibbons**. Mr. Koplan, what would you suggest the administration put in that bill? Or would you suggest there be a bill at all?

Mr. **Koplan**. We are not suggesting that there not be a bill to assist the Caribbean region, Mr. Chairman, but it is our feeling that more attention should be paid to a program with up-front assistance, such as what is being discussed in title II of H.R. 5900. That type of assistance, rather than trade and tax incentives that will encourage both U.S. industry and multinationals to pour investments into the region and thus diminish our own productivity and investment in the United States. And as I said earlier, the types of relief that are contemplated in titles I and III of the bill, as I understand it, are not the type of relief that, for example, Canada, Mexico, and Venezuela are contemplating. There must be a way to do this, and we would be happy to work with you, toward developing a program without sacrificing additional U.S. jobs and causing further flight of U.S. industry and others from the United States. And as I said, we would be happy to work with you to try to work something out.

Chairman **Gibbons**. I wonder if putting more up-front money, as you suggest there, wouldn't cause a sudden spurt of economic development in that area that may be harder to absorb than a slow development that, obviously, is going to come about eventually.

Ms. **Jager**. That really is an interesting question. The main problem that perhaps we don't give enough attention to in the statement is that there isn't anything really new in this proposal. We have supported over the last 30 years various types of proposals that theoretically would help countries to improve, and they have certainly been available in the Caribbean throughout the period. My reaction when I first saw the first draft of this was that I was too old to go through this again. The people there aren't going to be helped through this. And I don't think that it is up to the American labor movement to try to tell the administration that doesn't even believe in helping us at home how they should help people in other countries. But I do believe that for the administration to come to the Congress at this point and propose something that violates all of our international commitments, when they are telling us that any suggestion for changing legislation at home would be a violation of the GATT that would cause incredible retaliation, is just something I am unable to understand, Mr. Chairman. Everything that we ever propose for American workers is considered a sin and a violation under international trade rulings, but here you have admittedly an up-front—a violation of everything that the administration says it stands for in international trade. And it is going to go to the GATT for a waiver. I don't understand that. I don't understand why they don't know that out of this imports will be encouraged not necessarily from the Caribbean, but from the Far East or from any other part of the world without even touching the Caribbean, because that was the history with Soviet watches. And if you look at what was done with the Japanese cab chassis, all you need to do is put a couple of nuts, bolts and screws on two different parts and put them together and say it is 25 percent content and send it into the United States duty-free. I think the traders are much more intelligent than——

Chairman **Gibbons**. Well, they just transferred jobs from my constituency to somebody else's constituency. They happened to assemble those cab chassis in Tampa and they had a lot of jobs there, so I am not impressed with your argument.

Ms. **Jager**. I don't understand, Mr. Chairman.

Chairman **Gibbons**. The trucks are still coming in. They just assemble them in Japan now. And people used to do the assembly process in Tampa on the cab chassis. And it was more than putting a couple bolts in, too. I happen to know something about that. Of course, that is something to do with chickens, not anything to do with—you know, we have the highest tariff rate on trucks of any nation in the world. Nobody has a tariff rate as high as we do on trucks. I don't know why.

I don't think you picked a very good illustration.

Ms. **Jager**. Well, I only picked it because I thought it was dramatic, not because of the rate of the tariff.

Chairman **Gibbons**. It is dramatic.

Ms. **Jager**. What I am suggesting is whether the tariff is 3 percent on an auto or whether it is 5 percent on TV equipment, anything can now come in, whatever its sophistication, under this program, and I think that this is a trade diversion that makes a mockery of all your other legislation.

Chairman **Gibbons**. Comments that I have received from at least one head of government in the Caribbean about the past aid has been that the past aid has all been funneled through the governments in the Caribbean and the governments in the Caribbean were not only notoriously unstable prior to the aid, but the aid in effect really made them more unstable because the infrastructure was never built up in the islands.

And while I realize you have got to have harbors and you have got to have airstrips and things like that or you can't do any commerce in that area, I do think that we were perhaps inadvertently promoting a form of national socialism down there as far as economic development was concerned when we really hadn't intended to. We intended to try to stimulate the entrepreneurship of those islands, and in effect we were stimulating the fight over political control of the Caribbean rather than anything else by the past aid programs.

And the aid programs, frankly, have the same kind of direct economic impact as the trade programs have. They make one area highly competitive against another. You have got numbers in my area that are unemployed because of the aid program. About 4,000 people right now because of the aid program are unemployed because of foreign competition. So, you know, it is almost six of one, half a dozen of another kind of thing.

Mr. KOPLAN. Mr. Chairman, I don't say that the solutions to these problems are easy. I don't have a quick fix for it. But I do say that if the so-called trade and tax incentives are adopted, I don't think anyone here would dispute the fact that it is going to have a serious additional adverse impact on employment in the United States and on U.S. productivity. And it seems to be, taking the tax provisions, for example, it seems to be at counter purposes with what the arguments were for the so-called Economic Recovery Tax Act last year, which was to encourage—I mean the arguments for the business side were to encourage them to keep our money here, to invest in additional U.S. plants, additional U.S. machinery, additional U.S. equipment, and result in the additional U.S. jobs. But as I read the testimony of the administration witnesses that have preceded me during the course of your hearings, they have now turned that around and encourage them to go to the Caribbean Basin. And this has got to—you know, it has got to result in increased unemployment all over the U.S.—in Pennsylvania, in Florida, in Michigan, and Minnesota. I mean who isn't going to be touched by this? I don't know what the easy answer is. Sure, we are concerned with the situation in the Caribbean Basin, and we would like to see a responsible program worked out. But we don't see these types of so-called trade and tax incentives as the answer.

Chairman GIBBONS. Well, what's the answer?

Mr. KOPLAN. I don't know. I don't know what the answer is. But I think that there is a need to sit down and take another look at it, rather than just sweep through a proposal that for the next 12 years is going to result, admittedly, in increased United States unemployment when right now that figure is at about 9 percent in the United States and result as well in diminished U.S. productivity. We have been listening to arguments for the last year and a half to do away with the very things that are about to be created through titles I and II of the bill.

Chairman GIBBONS. Mr. Bailey?

Mr. BAILEY. Thank you, Mr. Chairman. First, all I have to say, Mr. Wolfe, is you have got to forgive me. I read part of your statement, I was back in my typically busy mind, read part of another, integrated two things, and I hate to say this, gave you more credit than I had intended to. But I did want you to know that.

Chairman **Gibbons**. I am glad you explained it. I almost fell out of the chair. [Laughter.]

Mr. **Vander Jagt**. I thought you were a sudden convert.

Mr. **Bailey**. I had to go down to a subcommittee meeting and get up and run out of the door. It must have really looked suspicious.

Chairman **Gibbons**. We are back on track, anyway.

Mr. **Koplan**. We were hoping you would be back, Mr. Bailey.

Mr. **Bailey**. So I goofed. Put that in the record, would you?

Chairman **Gibbons**. That happens to all of us, so don't worry about it. It is very difficult. All these type of things look the same.

Mr. **Bailey**. Well, I speed read and I mixed two statements here and had them caught between each other. I really apologize to you most humbly. I made a mistake.

I suppose I am prejudiced, I have very strong union sympathies. I don't think there is any doubt about that. I also have very strong free enterprise sympathies, and I think most of the business community knows how strongly I feel about their needs to reinvest, and I know that we have talked about that word productivity and what it means. And I would like to just comment that I also appreciate the honesty of what you said. When I got back from Vietnam, one of the things I have always treasured and kept was a very thick portfolio that I received—I personally wrote George Meany after I read some comments in the paper. George Meany had to be one of the most strident, committed, antisocialist, anticommunist leaders we have ever had in this country. Very strong believer in the rights of labor to organize, very strong believer in the free enterprise system. And it is a shame that we get at these things in our country and get a little confused in the fact that we are in the same boat.

And I want to compliment you on a statement that I think is excellent. I think the point that you are making is exactly the point that we as Members of Congress are going to have to explain to the American public: How we rationalize and how we explain the simple, plain, flatout elimination of semiskilled, in some cases low skilled jobs, to people that desperately need that income to eat, and we don't have programs to train or retrain, we want to zero them out and get rid of them. It is just plain not fair.

And in terms of the balance of what we stand for, it is an intellectual and a political and an economic hypocrisy.

Now, let's go to the side that you were commenting on in answer to the chairman's excellent question about what do we do. Well, I have the same difficulties, I have got to be honest with you, on exactly how to approach the problem. There is no doubt in my mind, you know, if they had come to this chairman and sat down and taken stock of these things and looked over them and put this idea out and floated it a little differently, I think we could come up with some kind of proposal to do something down there, to extend some of the benefits of this economic system which include the rights of people to organize, which include the rights of people to try to better themselves in their economic well-being. Those kinds of things have to go with these proposals when you go down there. You don't do something for America by just increasing a corporate presence. Businessmen will tell you that. I had a businessman who works down in Puerto Rico saying exactly the same thing yesterday. This is not going to transfer the kinds of things we associate with America's political culture that means so much as part of the economic rights and political rights that are a part of this system. I really don't think they will. He testified that real income in their operations to people in Costa Rica had dropped 15 percent. Now, in all fairness to him he said it had to do with the currency fluctuation thing, and I am going to check that out. I am sure the fellow was being honest, and I have no reason to doubt his word. But the point is in the face of the rising inflation you have got a real income drop and then you are going to go in there with a 60-cent-an-hour job, I don't know what you do for America. I don't know what you do for those people. I really don't know if you do that much at all for what the country stands for. And we do have problems in Africa, we have got problems in Asia. And I want to say that I do agree with you. I think that this thing has to be looked at in balance. It is not an issue of protectionism. It is an issue of equity and balance and trying to do something in a permanent kind of a way. It's unfair. And I very much appreciate your views, and I thank you for the balanced and fair way that they were presented because I think they honestly were and I respect you for representing your people. Thank you.

Mr. KOPLAN. I appreciate your comments, Mr. Bailey.

Chairman GIBBONS. Mr. Vander Jagt.

Mr. VANDER JAGT. Thank you, Mr. Chairman. Just one small point, Mr. Koplan. You said it was mystifying to you that the administration could propose this when we have a $3.2 billion negative balance of trade with the countries in the Caribbean Basin. Is it not true, if we exclude oil and petroleum products, that we have a favorable balance of trade with the countries in the Caribbean Basin?

Ms. JAGER. I don't know, frankly, whether—not oil, I think. I think that if you excluded bauxite and related products. But of course you can't exclude oil. You see, one of the reasons that the preference system was instituted originally was that the countries of the world said that they couldn't get foreign exchange. And one of the ways that they have gotten foreign exchange is through the higher price of oil and raw material. So that if in fact the trade balance would be shifted because of oil, which I don't have the figures before me and I don't think—it would be close, if anything. You may be correct. It could be—but in terms of what your objective is, the objective of helping the country, it wouldn't do any good at all. And we are now suffering from a new problem that wasn't there when we started proposing programs very much like this 30 years ago. I just find this not a very new problem, but a tragically old one.

Mr. KOPLAN. I think, Mr. Vander Jagt, that I also mentioned in that part of my testimony as a part of the basis for my comment that we now have a $40 billion trade deficit with the world, and that was also a reason for my making that comment.

Mr. VANDER JAGT. Yes. You said it was mystifying to you that the administration could even consider it when we have a $40 billion negative balance of trade, including a $3.2 negative balance with the Caribbean Basin.

Mr. **Koplan**. Yes.

Mr. **Vander Jagt**. And my question was—in fact, I will make it more specific: If you exclude oil and petroleum products, don't we have a favorable balance of trade of $317 million?

Ms. **Jager**. Yes, sir.

Mr. **Koplan**. Yes, sir.

Mr. **Vander Jagt**. Thank you. Thank you, Mr. Chairman.

Chairman **Gibbons**. Mr. Frenzel.

Mr. **Frenzel**. Thank you, Mr. Chairman. I want to thank the witnesses for their testimony.

On page 4 of your testimony, you say that if we have to use this tactic, the bill should have a higher content provision. How high should the content provision be?

Mr. **Koplan**. First of all, I don't want to——

Mr. **Frenzel**. 500 percent?

Mr. **Koplan**. No. First of all, I don't want to convey the impression that if we juggle the content provision that we are suddenly going to support the trade provisions in title I. That is why I wanted to couch my response——

Mr. **Frenzel**. So if we were to amend the bill, we should not do so under the illusion that you would some day support it. Is that correct?

Mr. **Koplan**. That is correct. But my point here, Mr. Frenzel, is that if we have a 25-percent content requirement that can be satisfied by lumping, you know, all of the countries in the region and, as I recall, Puerto Rico qualifies to be lumped as well, and collectively that adds up to 25 percent, I think it is called country of origin in the bill, that it will be relatively simple for multinationals to funnel U.S. imports through the Caribbean region. And I would just point to the fact again that in existing GSP law as I understand it, the 35 percent local content requirement that now exists suddenly rises to 50 percent when you start combining countries. So we are talking about a provision here that would be half of what the GSP legislation provides. And I see that as a problem.

Mr. **Frenzel**. Which answers the question which you posed to us as to why we didn't use GSP in the first instance. Both of you mentioned the watch problem. Would you tell us how many employees were involved in that huge operation in the Virgin Islands which by your statement put the watch industry out of business in the United States?

Mr. **Koplan**. I don't think that was our testimony.

Ms. **Jager**. I didn't know that we said that it put it out of business, Mr. Frenzel. I thought we said it contributed to it. The point was that the American watch industry claimed several years ago that this was a conduit area, this was a time in which the industry was in terribly bad shape, and I assume that it is in even worse shape now if it exists at all. I'm not aware of the current state of the industry. But I didn't——

Mr. **Vander Jagt**. It says the arrangement merely helped destroy the U.S. watch industry.

Ms. **Jager**. It was a help. It was just one more contribution. I am sorry if it left the impression that this was the only factor. That was not the intention. The point is you have a lot of industries that are having a lot of injuries, and each little injury from each little new provision to help imports in, adds up. Remember, these imports aren't coming in naturally under this. This is a funnel that is being created to help them come in without any protection at all.

Mr. FRENZEL. The problem is both of your examples——

Ms. JAGER. I think minimal job creation in the Virgin Islands, because there wouldn't be great job creations in the Caribbean out of the program through creating tax incentives. It just hasn't happened since we have had all these other programs. One lawyer in town told me that there were more jobs created in Washington trying to do something about the watch provision than there were in the Virgin Islands.

Mr. FRENZEL. I believe that, too. But I believe that both of your examples, the trucks and the watches, were rather dramatically overstated.

Mr. KOPLAN. Excuse me, but I thought that in my prepared statement—I didn't read that full paragraph into the record, but it did say the job creation in the Virgin Islands was minimal. I mean one of the points we are making with regard to the Caribbean Basin Initiative is that the real beneficiaries, as we see it, the way the bill is structured, will not be the people in the Caribbean.

Mr. FRENZEL. The problem with the watch industry illustration is that practically no watches are coming into the country from there. The industry has changed its nature. Nobody wants to read Russian sweep-hand watches any more; they want to look at nice digital displays. And so these folks don't sell any watches. They didn't contribute to the change in the industry. They were part of the ones who are the purple-hearted veterans of the change in the industry.

Ms. JAGER. Excuse me, Mr. Frenzel, but didn't the industry make that claim?

Mr. FRENZEL. Of course. Have you ever seen an industry that was in distress that didn't claim some awful foreigner ruined it?

Ms. JAGER. I have seen a great many leave the country. A great many in distress have left the country and they no longer express any concern at all about the United States.

Chairman GIBBONS. You made the statement about a $40 billion trade deficit, and I am not going to challenge that, but I just want to point out the AFL–CIO has a unit in some of these things. The manufacturing trade in the United States in 1981 had a surplus of $11.700 billion. In capital goods—and I guess the AFL–CIO had an interest in that last year—we had a surplus of $45.7 billion.

Mr. FRENZEL. If the chairman will yield, our deficit——

Chairman GIBBONS. Aren't you on the wrong side of this argument? The deficit in oil was $73 billion. Now, you know, sure we have got a $40 billion deficit, but, you know, on the manufacturing side you had a surplus of $11.7 billion. That is high-paid American jobs. On the capital goods side, some of your highest paid members are in that $45 billion surplus. Now, are we going to throw all of that away because you ought to be chasing the lemons?

Ms. JAGER. Mr. Chairman, our contention is that we are throwing that away.

Chairman GIBBONS. You are throwing what away?

Ms. **Jager**. I think the record shows that we are——

Chairman **Gibbons**. We never had surpluses that large——

Ms. **Jager**. The world is increasing its advantage over us. In a very large world we are losing—I think there is a contention by industry that we are losing the share all the time of a growing market for capital equipment, that we are being shut out of that market, and I thought——

Chairman **Gibbons**. We don't have a monoply on it, but we had a $45 billion capital goods surplus—we exported $80 billion, and we imported $30 billion. We have a surplus of $45 billion worth of goods in the capital goods area last year alone. That is high-priced labor, that is high-priced technology, that is high-priced everything. In the manufacturing trade we had a surplus of $11.7 billion. That is all generated because there are foreign markets out there. I really have a hard time following your arguments. I know you are trying to protect everything that is a member of your constituency, and I found out years ago you can't do that; I am elected like you are. But sure, we have a tremendous appetite for oil, and I hope one day we will cure it. We have a temporary problem—I think it is temporary, in automobiles. The Congress and all of us working together sent the American consumer the wrong answer in the 1970's about price controls—I, fortunately, didn't vote for them—on oil. So the American consumer went out and bought the gas guzzlers, and Detroit will eventually catch up. Sometime I believe they will. So we have got those problems. But I just——

Mr. **Bailey**. Mr. Chairman.

Chairman **Gibbons**. Yes, sir, go ahead. I would like to hear you, Mr. Bailey, on this. This is capital goods. A lot of them are manufactured in your area and manufactured goods I am talking about.

Mr. **Bailey**. I don't want to side against my chairman.

Chairman **Gibbons**. I don't care if you side. I just want to get the argument out on the table and maybe I will understand it better.

Mr. **Bailey**. Well, instead of absolute figures, you have got to look at the return on investment; you have got to look at investment, and you have got to look at trends. I think that is very true. You are looking at a nation that has an increased responsibility, for example, in the defense area. It is increasingly expensive to make the kind of investments in research and technology, the drain on brain power. I am viewed as one of the strongest supporters of a very strong contingent, and have an excellent voting record in that regard and I am going to continue to because it is vital.

Chairman **Gibbons**. I am not challenging you, but——

Mr. **Bailey**. Let me respond, because I think you raise an absolutely excellent question. The Nation has got a multitude of problems that it has to face and the trend is that we are not going to be able to maintain the kind of economy, and that relates to military security, that we have to because of investment trends, return on investment, et cetera. We talk about the Japanese situation, the European situation, and I think the example is very well put. I don't know where the AFL-CIO comes down on this. I had worked very hard, and I think you know that, in the area of alternative minimum corporate tax. I know where most of the Members of the minority side stand on that issue and many Members of the majority side. But it is ironic that the very kinds of changes we are making to make us competitive as a Nation with a competitive tax and regulatory structure to increase investment is going to make that trend even worse because there is an export of technology in many ways going on. I realize that we are very competitive and we shouldn't have a monopoly on these things but the United States has a right in terms of its tax structure to remain competitive, and we are not. So to get back over to the business side, the best things that were done in that tax package are now being recommended as being undone, and I think the union people here are making a point. I think they are right about that.

Chairman GIBBONS. Well, I don't say they are not making a point, but I don't know why—I almost detect that—you know, we can't sell these capital goods, we can't sell these manufactured goods unless somebody is buying them out there. If we keep selling and selling and selling, nobody will be able to afford our goods. They wouldn't be able to afford the capital goods or the manufactured goods, and the two areas in which you all have the greatest interest, I would imagine, would be in the capital goods and the manufactured goods, and in those two areas alone, in 1981 this country had a surplus of over $55 billion in foreign trade, surplus of over that much. Now, that is a tremendous figure.

Ms. JAGER. Mr. Chairman, I think your argument the way it is phrased is one that a great many people believe is the problem, and I think that part of the difficulty in understanding our position is the nature of trade today, so that the dollar value volume of the capital export is not necessarily reflective of the jobs or even of U.S. production. We wish it were. But in many of these cases the parts of these large capital equipment pieces, such as airplanes and whatever they want to include as capital equipment machinery, are in fact made in other countries and imported and——

Chairman GIBBONS. Well, they would be in the import statistics.

Ms. JAGER. But they would be stated at the foreign value and they would not be structured to sell at the same type of price, so that there is no actual match in this. We have faced this for a great many years. We have no statistical bases.

Mr. FRENZEL. You mean you don't know what comes in and what goes out?

Ms. JAGER. We do not have a count of it, no, sir. The Trade Act of 1974 asked for it and it has never been done.

Mr. FRENZEL. But you have import figures and you have export figures. Do you mean they are incorrectly stated?

Ms. JAGER. They are on different statistical basis and it is not identical.

Mr. FRENZEL. What is the different basis, please?

Ms. JAGER. Well, the import data are reported on the tariff schedules of the United States as the basis for that and it is based on foreign valuation. The export figures are based on U.S. valuation, and they come from census. But they are gathered differently. This has been a problem for a good many years. I am sorry about this, because I think it is genuinely confusing, but I do want to make the point that the job content is not really reflected necessarily by the dollar volume of trade.

Mr. BAILEY. Would the gentleman yield on that?

Mr. FRENZEL. I'm sorry. I didn't have the time. I interrupted.

Chairman **Gibbons**. That is all right. I will yield.

Mr. **Frenzel**. If I do, I yield.

Mr. **Bailey**. Thank you, Mr. Chairman.

One of the best examples of what we are talking about here are issues concerning domestic content, American percentage, buy America, those things, perhaps best illustrated by the situation that just developed in New York where the municipal authority made a purchase largely centered on the advantages in the financial arrangements of what was done, Mr. Chairman. A part of that contract will hopefully be going to American contractors. Much of that will be brought into the country, however; 50-some percent of that production will be offshore. What it does represent, Mr. Chairman, in percentage terms, is an increasing percentage of offshore capital goods production. Again, you know, it is an issue of trends and that kind of thing. Very ominous trends in many ways.

Chairman **Gibbons**. Well, I disagree. I don't like the position we are in. One of the reasons, of course, is our super-valuated dollar. I shouldn't say over-valued, because it probably is a correct recognition of what has happened. One reason—there are a number of reasons the dollar is high, but one of the reasons it is high is because we have been selling a heck of a lot more than we have been buying. Every currency in the world has fluctuated downward against the American dollar in the last year, and that is because America has had a more prosperous economy than the rest of the world and we have sold more than anybody else. That has been the principal cause. There are other causes, and I will admit there are, but I listen to all these stories about the problems we have, and obviously we have them in the automobile industry. There is no doubt about that. I think it is a problem that perhaps Congress is largely responsible for because of our unwise price control operations in the petroleum industry. When everything else was uncontrolled in the American economy, the petroleum prices were controlled and the American consumer got the idea that petroleum was cheap, and it wasn't cheap and so we practically shot down our own industry. But on the rest we are doing pretty good.

Mr. **Bailey**. Mr. Chairman, one example—and you know, I wouldn't argue with you, you have more experience than I do, but——

Chairman **Gibbons**. I am just reading the facts out of the Department of Commerce publication.

Mr. **Bailey**. See, I have gotten into this thing with capital intensive industries in particular. You look at specific examples, we are building ultramodern rail facilities, not in the district any more, but secondary utilization of raw steel production for ultramodern rail facilities the capital goods and equipment of which were furnished from Japan. At the same time we have a firm back in Pennsylvania that produces very high quality ceramic steel rolls that may last longer, they are a good production item. We attempt to peddle that capital good, primarily, incidentally, in Japan or in Europe because it is a superior product, it is recognized and acknowledged to be, and you can benefit that market there because they don't want to detract from those jobs there. I think this is where the problem comes with capital percentage—capital goods and some of the drop-off in the trend. That is an antiproductivity mechanism in itself imposed in other countries and in nontariff ways. I think this is really what is at the core of the problem. I don't think anybody argues that we have to have this independent involved world economy based on comparative advantage, but the real world doesn't seem to work that way.

Chairman **Gibbons**. You point out the train. I hate to take up the time of the other witnesses, but let's point it out. What is the difference between the train situation. The Japanese are in my State today trying to sell a train. Nobody in my State really wants a train, but the Japanese are trying to sell a train, and they are probably going to create a demand for it. But you know what is happening? If my people wanted a train they couldn't find anybody in the United States that would build them one.

Mr. **Bailey**. That is the point I was making.

Chairman **Gibbons**. The Japanese are there trying to create a demand for a train.

Mr. **Bailey**. Yes, sir.

Chairman **Gibbons**. They are going to sell a train eventually there.

Mr. **Bailey**. I would love to answer that.

Chairman **Gibbons**. Go right ahead.

Mr. **Bailey**. OK. Because I have studied the problem. A good example was on that MTA deal in New York there was an attempt to get Pullman to resuscitate itself and actually get into this business in terms of a bid on a large volume of cars, but you know why a company in this country won't do that? A perfectly good example, Mr. Chairman, is the ultramodern rail facilities. If you are sitting out as a businessman in this country and you want to make an investment especially in a long term capital-intensive area, there is so much unpredictability, there is so much risk that you are just flat not going to do it. We have got the same thing with mineral deposits, and that train is the best example. It is Government policy and our fault. It is not our business people's fault and it is not our labor's fault, and the Japanese, I would like to sell them a lot of things too. You can't even sell them a pack of cigarettes. But on capital goods, I think the attitudes of other governments and tax structures towards capital goods, it is eventually just going to erode our capacity to the point where we are not going to be in a lot of those businesses. If we shouldn't be because we sell high technology goods and services, that is one thing. But military security is going to suffer if you don't have a vehicle industry and if you don't have a certain percentage of steel production upon which to rely. At some point you become very insecure and vulnerable and that is my concern.

Chairman **Gibbons**. We are not exactly going out of business. We sold $80.2 billion worth of capital goods in foreign markets last year. That is the highest figure that I know of. We never did that kind of trade before in foreign markets.

Mr. **Frenzel**. If the chairman will yield, the last time we were talking about trains in this subcommittee we were talking about box cars, and these folks came in and testified against letting Mexico maintain GSP on box cars when we had tens of thousands of them backlogged from American producers.

Chairman **Gibbons**. Well, thank you all for coming. I appreciate it.

Mr. **Koplan**. Mr. Chairman, I just want to make one last comment.

Chairman **Gibbons**. Surely.

Mr. **Koplan**. When we go back to 9.6 million unemployed American workers, are we to tell them that this legislation is going to diminish that figure, or is it going to increase it? I think that is a question that has got to be dealt with.

Chairman **Gibbons**. I honestly don't think this legislation would have any impact on it one way or the other.

Mr. **Koplan**. You don't?

Chairman **Gibbons**. No.

Mr. **Frenzel**. Do you have any figures on it?

Chairman **Gibbons**. I think the unemployment rate in this country is driven by forces that are far larger than this bill.

Mr. **Koplan**. But are you saying this bill will not contribute to higher unemployment figures, Mr. Chairman?

Chairman **Gibbons**. No, sir, I don't believe so.

Mr. **Koplan**. You don't believe it will.

Chairman **Gibbons**. No.

Mr. **Koplan**. Then we have an honest difference of opinion, Mr. Chairman.

Chairman **Gibbons**. Well, I think all of our differences are honest.

Mr. **Koplan**. I wasn't implying otherwise.

Thank you, Mr. Chairman.

Chairman **Gibbons**. Thank you, sir.

Mr. Alexander, we welcome you here. We know of your interest in trade and the responsible position you hold in the Democratic leadership of this Congress.

STATEMENT OF HON. BILL ALEXANDER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ARKANSAS

Mr. **Alexander**. Thank you very much, Mr. Chairman and members of the committee. Of course I thank you for the opportunity to be here to testify and discuss the administration's proposed Caribbean Basin Initiative, and I have a prepared text and request permission to submit the text and to refer to it in part.

Mr. Chairman, the last witness that was here raised the question to which I address my remarks, the question of whether or not the Caribbean Basin Initiative of the administration tends to increase unemployment in the United States, and before I answer that question, I would like to say that as one who has traveled throughout the Caribbean area and in Central America on numerous occasions and have many friends in that entire region, and one who realizes the strategic importance of the stability of that region to the security of the United States, that I support a Caribbean Basin Initiative. I do not support it, however, at the expense of the people whom I represent.

Chairman **Gibbons**. I understand.

Mr. **Alexander**. In Arkansas, in my congressional district, there are 16 shoe manufacturing plants which employ approximately

5,000 people, whose jobs are threatened by this initiative. Now, there are very good reasons for the President's initiative, but according to the publications of the Bureau of Labor Statistics, not only are the some 5,000 jobs in the First Congressional District of Arkansas threatened by the Caribbean Basin Initiative; about 143,000 workers employed in the footwear industry in about 700 factories located in 37 States are likewise threatened by the initiative. It is a small industry and one that locates its factories for the most part in small and medium-sized towns located in the heartland of this great country. And I expect that those locations in the First Congressional District in the northeast region of the State of Arkansas are fairly typical of the kinds of towns and communities in which these factories can be found.

The New England, mid-Atlantic, Midwest, and Southern States share equally in the production of footwear with each of those areas contributing about 25 percent to the total production.

In this Nation, the footwear industry employees turn out 375,000 pairs of shoes a year. About the same number of shoes is imported into the country every year from foreign producers. Those facts have changed significantly over the last 20 years as the imports have dramatically increased during that period of time.

If the Caribbean Basin Initiative is enacted in its present form, which excludes duties on shoe imports produced from that region that would be sold and imported into the United States, we expect the present equality of production that exists within the United States and without the United States to change dramatically.

The problem that I have with the Caribbean Basin Initiative is that it ignores the fact that footwear is a highly import-sensitive industry. The International Trade Commission has recognized this fact on previous occasions by ruling twice that imports seriously injure the domestic footwear industry. Congress acknowledged that fact by including nonrubber footwear in a list of articles excluded from eligibility from the GSP under the Trade Act of 1974. But the administration's proposal ignores and refuses to acknowledge the fact that these footwear imports would cause the domestic footwear industry great harm and injury. In fact, it is almost predictable what injury would occur. I have not had the opportunity to analyze it to that extent, but it is a subject that I will spend some time with.

In my district, Mr. Chairman, we all know that whether we like it or not, that all politics is local, and those of us who support free trade and the expansion of trade have to reconcile our own representation of our districts with the overall grandiose goal of more trade throughout the world. And I certainly do not retreat from that goal, as I know the chairman and other members of this committee do not retreat, either. But it is a personal matter when 5,000 jobs in Arkansas are threatened by the administration's Caribbean Basin Initiative, especially in a situation where the unemployment in the State of Arkansas is at a 50-year high. Unemployment now ranges about 12.3 percent statewide, and in one of my counties, a county in which one of these shoe manufacturing plants is located, we experienced 22 percent unemployment. More than 3,350 people lost jobs in 1 month's time in my congressional district, and just today, the Wall Street Journal published an article, which I have not read but am told about, and I would ask permission to include some excerpts from that article as a part of my testimony.

Chairman GIBBONS. Certainly. You may.

Mr. ALEXANDER. The story is on unemployment, and it says that in parts of Arkansas layoffs passed levels in Detroit. And of course we hear a lot more about Detroit because the automobile industry has a greater visibility in our economy. And if the problem in Arkansas is greater than it is in Detroit, I submit that it is a great problem and that it would be compounded by this proposal that is pending before this committee.

[The following was subsequently received:]

The following are excerpts from an article appearing in the Wall Street Journal, March 25, 1982, which Congressman Alexander requested be included in the record. Chairman Gibbons authorized the additions.

"Shadows across Sun Belt employment show up clearly here in Arkansas. Though it calls itself the 'Land of Opportunity,' the state posted in January the highest unemployment rate since it began keeping records in 1950: 12.6 percent. The rate fell somewhat in February because of better weather—to 11.4 percent—but that is still far higher than the national rate of 8.8 percent.

"Some parts of the state are suffering even more than many Northern cities that have become well-known symbols of unemployment. Detroit, battered by the auto slump, had 15 percent of its workers jobless in December. Nearby Flint, Mich., had 16.5 percent. But here in Malvern, in Central Arkansas, the January jobless rate was almost 25 percent. In Trumann, in the northwest, the rate was almost 19 percent.

"We're surrounded on three sides by energy states, but we aren't one, explains Ken Coon, the administrator of the Arkansas Employment Security Division. 'And our economy is tied to agriculture, housing and automobiles—the three sickest parts of the economy.'

"But unemployment has spread elsewhere, too—a fact illustrated by the growing number of Sun Belt states qualifying for extended federal unemployment benefits. These supplement normal jobless payments and are granted only in the most drastic cases. Since Jan. 1, Nevada, California, Mississippi, Alabama, Tennessee, both Carolinas and Arkansas have joined 17 other states qualifying for the aid."

"Back in Arkansas, Malvern is suffering through one of its worst spells of unemployment in years. 'We're getting a quarter of the jobs we normally get,' says Clarence Copeland, the manager of the Employment Security Office here. Most of those are ill-paying and short-term jobs, he adds, such as raking yards and spading gardens.

"The layoffs have an especially servere effect on former workers at Reynolds Metals, because they can't find jobs that will pay the same high wages of $20,000 to $30,000 a year. Some laid-off workers now are earning $4 an hour at odd jobs, Mr. Copeland says. And many employers are reluctant to hire Reynolds' castoffs, adds Mr. Whitherall, because they know that if the company recalls workers, most will return for the higher pay. 'People resent you because you made so much,' Mr. Whitherall adds.

"The effect ripples through nearly every business in this town of 10,163. At the Malvern Daily Record, publisher Gene Chambers says daily display advertising in January fell 10 percent from a year earlier. Classified ads have stagnated, too. Last month, the paper ran free adds for people who couldn't afford the fee of $4 or so but 'need to raise cash by selling a cow or a milk-goat or a bicycle,' says Mr. Chambers.

"At a hamburger stand owned by Mayor Scrimshire, January sales dropped about 17 percent to $10,000 from a year earlier. 'We knew we were in trouble on Christmas Eve,' the mayor says. 'Usually we are making hamburgers until midnight, but this time we could have closed at sundown.'

"Laborers suffer, too. On a drive through town, Michael Ray Gatlin, a 20-year-old brick and cement layer, points out a rare house under construction. 'Pouring the footing for that was the last job I had, and that was over a month ago,' says Mr. Gatlin, who lives with his parents. 'There ain't no work around here, man . . . I'm getting out.'

There is similar sentiment in Trumann, where the jobless rate was already about 19 percent when Singer Sewing Machine Co. recently decided to close its plant, idling the last 600 workers it had employed there (The plant once employed 2,000.)

> Trumann and its surrounding county will lose $100,000 a year in taxes from Singer. T. R. McKinnon, an economics professor at the University of Fayetteville, says Trumann (population 6,405) is one of several small Arkansas communities that may become ghost towns as jobs leave and people follow.
>
> "When will employment rebound here? Experts say the state's economy will surge again as the nation's does, perhaps with some lag because of Arkansas' dependence on autos and farming. 'There will be a recovery,' say Mr. McKinnon, the economist, but he adds that one important factor in its strength and timing is the 'transition' that is taking place in Arkansas industry.
>
> "In the 1950s and 1960, he says, the state lured labor-intensive industries such as clothing manufacturers and shoemakers. Now those industries are moving to havens of cheaper labor in Asia and Mexico. To compensate, he says, the state must now attract more capital-intensive industries such as electronics. 'but right now we're caught in a transition period that is hurting,' Mr. McKinnon says."

I think that pretty well states my position, Mr. Chairman. Maybe at that point I could go into the production of footwear that has increased by way of import into this country from Singapore, Bahamas, Central America, and so on. But those facts are well known to the committee. Maybe I should conclude by emphasizing my opposition to the escape clause in the Caribbean Basin Initiative plan and stand ready for questions from any of you.

Chairman GIBBONS. What type of shoes do you manufacture in Arkansas?

Mr. ALEXANDER. All types.

Chairman GIBBONS. Leather and canvaswear?

Mr. ALEXANDER. Yes, and plastic. A lot of the shoes that are manufactured there are exported, and we manufacture athletic shoes that are exported into the western European market. I expect some of those people put another stamp on them and send them back over here and sell them, as many of our foreign competitors do. But all types of shoes, men's, ladies', high fashion, everyday shoes, just every type that you can imagine.

Chairman GIBBONS. Mr. Bailey?

Mr. BAILEY. Thank you, Mr. Chairman. I thank the gentleman from Arkansas. I always worry about being misunderstood, I suppose. We do have to make some changes and make some improvements, but it is simply unfair, it is unjust, and it cannot be rationalized that you would go to an American worker anywhere in this country and say to them simply, I'm sorry, you are expendable, you, your job, whatever, you are gone, and they go.

It is easy to talk about nameless, faceless masses of workers, particularly when they are in a small group and I could not agree with you more. If these changes are going to be made, if they somehow operate in the interest—and this initiative really does not address the true issues of trade that I happen to think the chairman has been very properly responding to and trying, struggling to learn more about and be able to answer. It is not in terms of economic efficiency and that type of thing. It is just simply a way of transferring some higher paid jobs here to a lower paid job environment. I don't think politically it is going to transfer that many of Americana. I honestly don't believe that it will. I don't know what the benefits will be, but it is unfair and unjust because we don't even have the mechanisms in place in this country to look after these people and their concerns, and a lot of people don't understand. Pennsylvania has a high rural population, and when you get out to a patch somewhere—and that is a word, I don't know if you use it down in Arkansas, but you go out somewhere to a patch and you see the impact of structural unemployment in those areas and what it does to people and their hopes and aspirations and their kids, then it hurts, and it hurts one person and it hurts all of us. I think the point you are making about concern for those people and their rights and interest is 100 percent valid. I want you to know that.

Mr. ALEXANDER. The only reference I have heard to patch is cotton patch, and that is why those people are working in shoe factories. They are trying to get away from cotton patches. The conditions in shoe factories are far better than, in their minds, the patch to which we refer.

[The prepared statement follows:]

STATEMENT OF HON. BILL ALEXANDER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ARKANSAS

Mr. Chairman and members of the subcommittee, thank you for giving me the opportunity to appear before you today to discuss the administration's proposed Caribbean Basin initiative and its implications for the footwear industy of our nation and more specifically the footwear industry in Arkansas.

You have heard from many witnesses this week who have told you of the benefits or disadvantages the acceptance of the President's proposal will have on their industry or group. The list of witnesses you have heard clearly demonstrates that your subcommittee is recognizing this issue as one that requires your careful consideration. I thank you for devoting your time and attention to this matter.

In the interest of conserving your time, I would like to summarize my statement and ask that the full text be included in your hearing record.

SUMMARY

First, let me say that I applaud President Reagan for the leadership he is offering in presenting the opportunity for economic progress to our neighbors of the Caribbean region. For decades the United States has taken for granted its trade relations and security position in the Caribbean Basin.

While I generally support the President on his Caribbean Basin initiative, I do have reservations about specifics of the proposal. I am here today to ask that footwear be excluded from the list of products eligible for duty free treatment from countries designated as beneficiaries of the Caribbean Basin initiative.

There is a very good reason for excluding footwear from the duty free imports status. To allow the duty free status on footwear could mean loss of jobs in the footwear industry at home. Development initiatives in the Caribbean area could result in the export of much needed U.S. employment.

According to publications by the Bureau of Labor Statistics there are approximately 143,000 workers employed in the footwear industry in about 700 factories in 37 states. It is a small industry and an industry that locates its factories, for the most part, in small or mid-sized towns such as those typical of the district I represent—the First Congressional District of Arkansas.

The New England, Mid-Atlantic, Mid-West and Southern States share equally in the production of footwear, with each of those areas contributing about 25 percent of the total U.S. production.

In this nation, the footwear industry employees turn out 375,000 pairs of shoes a year. About that same number of shoes is imported into this country every year.

As you can see from those figures, imports are a significant threat to our nation's footwear industry. What we are talking about, gentlemen, are jobs. President Reagan's proposal to allow duty free imports of footwear into this nation from the Caribbean Basin area is, in essence, exporting jobs that are needed here at home.

The problem that I have with the Caribbean Basin Initiative is that it ignores the fact that footwear is a highly import-sensitive industry. The International Trade Commission has recognized that fact by ruling twice that imports seriously injure the domestic footwear industry. Congress acknowledged that fact by including nonrubber footwear in a list of articles excluded from eligibility for Generalized System of Preferences under the Trade Act of 1974. But the Reagan Administration refuses to acknowledge the injury imports will cause the domestic footwear industry.

The argument by the Administration that footwear manufacturing is presently limited in the Caribbean Basin does not comfort me. The argument by the Administration that footwear manufacturing will not be an industry they will encourage in that area, likewise, does not comfort me.

I don't accept those arguments because developing countries can easily enter the footwear manufacturing industry and existing small operations can expand quite easily. The industry requires only semi-skilled workers, who are readily available in developing countries. In addition, the footwear industry in the U.S. is at a disadvantage because developing countries can provide workers at low wages. The combination of semi-skilled workers and low labor cost available to the Caribbean nations make the footwear industry one they cannot resist especially if they are given the extra incentive of duty free access to the U.S. market.

I agree with the Administration that we need to be supportive of our neighbors, but not at gret expense to ourselves.

There are 18 footwear manufacturing plants in my district. Those plants employ between 4,500 and 5,000 people. In one county in my district 56.8 percent of all those employed in manufacturing are employed in the footwear industry.

In my district we cannot afford to see any footwear employees in jeopardy of losing their jobs. During January the average unemployment rate for the 24 counties in my district was 15.4 percent. In one month's time between December, 1981 and January, 1982, 3,350 people in my district lost jobs.

I picked up the Wall Street Journal this morning to see a story on unemployment that carried a sub-heading which read "In parts of Arkansas, layoffs pass levels in Detroit." Arkansas posted in January the highest unemployment rate since it began keeping records in 1950; 12.6 percent. The rate fell somewhat in February—to 11.4 percent, but that is still far higher than the national rate of 8.7 percent.

I urge all of you to read that article so that you will understand what is happening to the small and mid-size towns of this nation.

The people employed in this small industry, however, do not look for relief from the Reagan Administration. This administration has demonstrated a reluctance to help small industries and at the same time a willingness to help larger industries. The smaller industries are asking Congress for help.

I have already mentioned that the ITC has ruled that imports severely injure the footwear industry. The ITC made that ruling twice, the last time was last year and the decision was unanimous. But the Reagan Administration rejected the footwear industry's request for an extension of limitations on imports from Taiwan and Korea.

However, the ITC ruled that the automobile industry was not severely injured by imports and despite that ruling the Reagan Administration negotiated an agreement with Japan to limit automobile imports.

There are other examples of favoritism being shown by the Administration to larger industries. The Administration is allowing an exemption for the textiles under the Caribbean Basin Initiatives duty free imports. The result is that those Caribbean nations that manufacture cloth uppers used in the footwear product will be encouraged to expand into footwear. Textiles, a big industry, will have an exemption at the expense of footwear, a small industry.

The Commerce Department has reopened trigger price mechanism hearings on cases filed by the steel industry. The steel industry is a big industry and it is getting recognition from the Administration.

The people in those 18 plants in my district should not face the threat of losing jobs because the Reagan Administration ignores small industry.

POTENTIAL FOR IMPORTS

We cannot ignore the fact that the Caribbean Basin area already has the potential to develop its footwear industry. Current shipments from the region are only at 2 million pairs now, but historical trends indicate that a country can increase footwear exports dramatically in a very short time.

Just one example of that, and there are many, is that imports from Singapore jumped from 1,000 pairs in 1977 to almost 4.5 million pairs last year, according to reports from the Foreign Trade Division of the Commerce Department.

Numerous Caribbean countries already have a footwear industry. They include the Bahamas, Costa Rica, the Dominican Republic, El Salvador, Guatemala, Haiti, Honduras, Nicaragua and Panama. Many are relatively small, but again comparatively low capitalization requirements make expansion of capacity easy and the potential for rapid production expansion great.

I have already noted that there are about as many pairs of shoes imported into the U.S. as are produced here. Let me point out that imports into from the Caribbean Basin, if they follow traditional trends, will not merely displace products from other importers.

There has been some displacement of imports, but the predominant effect of higher imports has been to reduce domestic production.

Between 1968 and 1976 imports from Taiwan and Korea rose by 183.7 million pairs and imports from the rest of the world did not decline. Instead, domestic production fell by 220 million pairs. It was at this point that the International Trade Commission declared that imports seriously injure the domestic footwear industry.

I have said that imports continue to capture roughly one half of the domestic footwear market. This is the highest import penetration rate of any industry this size. As late as April of 1981 the ITC was still saying that footwear imports are injuring the domestic footwear industry.

THE LOOPHOLE

The Caribbean Basin Initiative will provide a loophole. The Dominican Republic and Haiti are the second and third largest suppliers of unlasted footwear uppers and of rubber, plastic, cotton and fiber uppers. Cotton and fiber uppers will not receive duty free treatment. As I have noted, the textile industry has an exemption. However, if these uppers are converted to higher value finished footwear, the finished product will enter duty free under the CBI. This is not only a loophole for producers of uppers, it is in fact, an incentive that they expand to full footwear production in order to avoid the duties.

THE UNITED STATES—AN OPEN MARKET

I would not be so concerned about imports taking jobs from footwear employees in America if not for the fact that the U.S. is the largest and most open market for footwear in the world. Our tariffs on nonrubber footwear are among the lowest in the world.

The one non-tariff trade barrier applicable to shoes, the American Selling Price, was abolished last year. In contrast, many of our trade partners impose non-tariff barriers. Canada has imposed a global quota on footwear imports. Mexico requires licenses on all footwear imports. In the Philippines, importation of footwear is not allowed at all. Japan has a severe quota on all leather products.

Some Caribbean nations have tariffs on shoe imports that are so high Congress is considering reciprocity legislation—even as we consider the Caribbean Basin Initiative, which will allow duty free imports of their footwear. In some cases, Caribbean nations have embargoed our footwear imports to them and yet we are considering opening the doors to our market without any duty.

The footwear employees of this nation—in Bastesville, Blytheville, Clarendon, Corning, Fisher, Harrisburg, Jonesboro, Leachville, Manila, Monette, Osceola, Paragould, Piggott, Pocahontas, Walnut Ridge, Wynne, DeWitt, and Stuttgart, Arkansas, and wherever else these plants are located, cannot afford to help the Caribbean nations develop their footwear industries at the risk of their own jobs and while those same nations show no sign of a reciprocal willingness for non-restrictive trade.

ESCAPE CLAUSE

The Administration's "escape clause" offers no escape for the footwear industry. The escape clause procedure is offered to safeguard domestic industries from injury under the Caribbean Basin Initiative. Non-rubber footwear does not qualify for this clause until July of 1983.

When the ITC ruled last year that the footwear industry was severely injured by imports, it recommended that the limitations on imports from Taiwan and Korea's footwear producers be continued for two years. So, ironically, the Administration is proposing to allow importation of footwear during the very time period that the ITC said our domestic footwear industry needed relief.

I urge you to take footwear off the list of items to be afforded duty free treatment under the Caribbean Basin Initiative and give the footwear industry a chance to survive.

Mr. Bailey. I thank the gentleman for a very honest reflection of the human side of the problem.

Mr. Alexander. I have no choice but to fight with everything I have got within me, and that is what I intend to do.

Mr. Bailey. I can't argue with that.

Chairman Gibbons. Mr. Frenzel?

Mr. Frenzel. I want to thank the witness for his testimony.

Bill, do you think the whole thing should go, or shoes should be exempted from it, or that shoes and other things should be exempted from it?

Mr. Alexander. Well, first of all, let's back up and ask the question do we need a Caribbean Basin Initiative? The answer is yes, no question about it. Our welcome to that area of the world is vital to our strategic interest, and political and economic stability is a key to that. If you don't do something, take some incentive, it is predictable that the region will follow the temptations that we have seen demonstrated in Nicaragua and now in El Salvador. So we have no choice but to approach it from a comprehensive basis. Now, we jump from there and ask the immediate question should that be achieved at the expense of displacing American workers, and the answer, in my judgment, is no. Then we have a middle question that we could ask: Should we achieve that by giving to American industry the opportunity to compete with the Caribbean region on an equal basis, and the answer is yes. I think that any industry in this country given the same circumstances should be able to compete with our counterparts, and I feel very strongly about that.

Now, we have industries that are not now equipped to compete, like the automobile industry. That is one industry that has not competed for various reasons, partly management. I think you could ask the same question about the footwear industry, and it is not able to compete because it is not competing with the Caribbean region on the same basis. So I say if the initiative is to include footwear, the initiative should be so comprehensive as to embrace whatever changes are necessary to allow Americans to compete with the Caribbean on the same basis. Therefore, I would conclude that the Caribbean Basin Initiative is incomplete in its present form and needs thorough examination and amendment before it is complete and before it should be submitted.

Mr. Frenzel. Would you be a little more specific? Is the reason that we cannot compete principally a difference in labor costs?

Mr. Alexander. I don't think that is the only reason, Bill. I think that probably the tax laws in this country have discouraged—prior to 1981 discouraged—the modernization of equipment that would improve our efficiency, that would allow labor savings, that would allow more efficient production and therefore better competition. Labor costs are a factor.

But what will happen if you allow this to go through? Americans that have the know-how will move to the Caribbean and invest to take advantage of the tax loopholes provided in this initiative—and it is a beautiful investment opportunity. If I wasn't a Member of Congress, I would be enticed to invest myself. So you take American capital and you move it to the Caribbean, you invest in a manufacturing plant that is able under present circumstances to produce at cheaper rates because—under the present circumstances because of lower wage rates, and you send those shoes into the United States, the same people make the money that invest, but it is at a net cost of the loss of jobs in this country. I think you need a total analysis of the problem in order to allow our people to be given some opportunity to compete.

Let me just throw one right off the top of my head if you are asking me to address the question of labor cost. Let's suppose for discussion purposes that is the only reason that we are unable to compete with them. Well, I think we should—in that instance—make a tax policy change that would give to the shoe industry the opportunity to give a double deduction, maybe, for wage rates which would permit the industry a profit incentive for staying here and that would permit them to be on a competitive basis with the Caribbean people. You know, that is just one technique that could be used that I have not previously thought out or thought through, but it demonstrates to me the need for a comprehensive approach, rather than a limited cursory approach that we are examining here today.

Mr. **Frenzel**. Are you aware of other commodities which trouble you besides shoes, Bill?

Mr. **Alexander**. I am only aware of the sugar problem. I sought and was invited to attend the President's speech before the OAS, at which time he unveiled his plan, but I have not seen the entire proposal and am not familiar with the total plan, no.

Mr. **Frenzel**. Thank you very much. Mr. Chairman, I yield the balance of my time.

Mr. **Bailey**. Mr. Chairman. I share your analysis, and I think the gentleman from Minnesota and the gentleman from Florida want to do something about this situation. I think politically all of us do. But I think it has to be balanced. I particularly appreciate the remarks that you made concerning the need for tax law changes for modernization of plant and equipment in this country. This may be an unfair question to ask because not being on this committee you probably don't get to study these things much. But the administration is seeking to make some changes that especially in the area of business taxes generally directly impact on that, involving a concept sort of like a targeting or channeling of moneys for investment opportunities for improvement of capital goods and equipment. They in short want to impose an alternative corporate minimum tax. Now, as I understand it, that is politically motivated. But it certainly is not motivated in terms of what this country needs. Do you have any reaction on that?

Mr. **Alexander**. I don't know enough about it to respond.

Mr. **Bailey**. I would hope that you would look into that, because that is precisely the area that we need help in in this country, to modernize plant and equipment.

Mr. **Alexander**. If you give people in this country an opportunity to make a buck, they will do it. It works every time.

Mr. **Bailey**. It sure does. All around the world.

Mr. **Alexander**. That's right.

Mr. **Bailey**. I thank the gentleman. I yield back my time, Mr. Chairman.

Chairman **Gibbons**. Fine. Thank you.

The committee is going to have to recess now, and we will resume again at 1:30.

Mr. **Frenzel**. Mr. Chairman, in case I might miss some of the afternoon's hearings, Mr. Bafalis asked me to put some questions to some of the witnesses. May I include those for the record and have the witness answer them later?

Chairman Gibbons: Yes. Thank you.

[Recess.]

AFTERNOON SESSION

Chairman GIBBONS. Unfortunately, because of the long dialog we had this morning, I am running out of time. I have until 2:30 for my next appointment, so I would ask Mr. Nicholas Kominus to come forward, please, U.S. Cane Sugar Refiners' Association. You may proceed as you wish, sir.

STATEMENT OF NICHOLAS KOMINUS, PRESIDENT, UNITED STATES CANE SUGAR REFINERS' ASSOCIATION

Mr. KOMINUS. Thank you, Mr. Chairman.

Mr. Chairman, our association represents all of the Nation's independent cane sugar refiners. Independent cane sugar refiners are not involved in the production or processing of sugar cane or sugar beets. They refine sugar that is produced in the United States and sugar that is imported from foreign nations.

Mr. Chairman, I appear here today to endorse the admirable goals of the President's Caribbean Basin Initiative. In so doing, however, I must say that we believe that these goals will not be fully attained unless the structure of the program, as it applies to sugar, is modified. Indeed, as presently structured for sugar, the program could have a negative impact upon the nations of the basin in the future.

In addition, the initiative could, if not modified, interfere with USDA's sugar program and generate other unintended problems. The problems involved are not insurmountable. The program can easily be modified so as to enhance its chances for success.

The administration has recommended that sugar imported from the nations in the basin be granted duty-free status.

We recommend to the subcommittee that it modify that proposal by providing for the collection of the duty, and for the subsequent rebating of that duty on a government-to-government basis.

The administration has already established the precedent for this approach under the initiative by recommending to the subcommittee that the excise tax on rum be rebated to Puerto Rico and the Virgin Islands.

We believe that the rebate approach is far superior in that it will: first, provide the governments of the basin with more control over economic development; second, insure that the full benefit of duty-free status is attained; third, lessen the need for even higher import fees on imported sugar, including sugar from the basin; fourth, lessen the chance that our Government will have to acquire sugar through the forfeiture of loans under USDA's sugar program; and fifth, lessen the possibility of the Government eventually being forced into an even more restrictive program on imported sugar in order to protect USDA's program.

Under the rebate approach, the benefits of duty-free status would be received by the governments of the basin rather than by the sugar producers. The governments can redistribute the benefits to the sugar producers and others in a manner they believe will attain development goals.

We believe the government-to-government approach is far more appropriate, particularly because one of the goals of the Initiative is to diversify away from sugar and not to encourage more sugar production.

Based upon the experience of the past, and our expectations for the future, we believe that only part of the total benefit will actually get to the nations it is intended to. The full benefit will undoubtedly not be attained, because once duty-free status is granted the producer has an added opportunity to discount the price of sugar he offers, if need be.

It is difficult, if not impossible, to estimate the extent of the discounting. Under certain circumstances it could, however, be substantial.

In the recent past, when the duty was just .625 cent per pound, discounting was nominal. The duty has, however, just recently been increased to the statutory maximum of 2.8125 cents. This provides the producer with a considerable sum, and he may under certain circumstances feel compelled to negotiate away a good part of the savings in duty in order to secure a sale.

It is our understanding, for example, that Thailand's loss of duty-free status under GSP as of March 31 led to considerable discounting on its part to insure shipments. If implemented, the Initiative will greatly expand the tonnage and the percentage of sugar that qualifies for duty-free status. As a result, it is estimated that well over half of our annual sugar import requirements could be met by duty-free sugar.

In addition to the large duty and the increased tonnage and percentage of sugar that would qualify for duty-free treatment, the situation will be further aggravated by the continuing decline in import demand. Thus, the competition among nations to ship sugar to our contracting market will intensify.

We would, therefore, expect discounting to be more of a problem in the future than it has been in the past.

Under all of these circumstances we believe it will be difficult for the basin nations to enjoy the full benefits of duty-free status.

The duty rebate approach would lessen the pressure to discount and increase the probability that the full benefit of duty-free status would be attained.

The administration recognized the problem of discounting when it established the import fee on December 22, 1981. It built into its import fee structure a factor of one-half cent a pound to account for discounting. As a result, the import fee on sugar from all nations, including those in the basin, is one-half cent a pound higher than it would be if there were no GSP.

The market price, despite the imposition of large duties and fees, has failed to attain the Government's price objective of 18.58 cents a pound, in good part because of the discounting under GSP. The additional quantity of sugar that would be available for duty-free status under the Initiative might force the administration to build even more than the present one-half cent into its fee structure. If it does, import fees paid by all producers, including those in the basin, would have to be higher. In this regard the Initiative would tend to be self defeating. What's given with one hand would be partially taken back with the other.

Here I might add, Mr. Chairman, that it is going to be difficult for the Government to estimate the amount they should build into the fee structure for discounting. I suspect that if they err, they will want to err on the high side so as to be sure that they will not acquire any sugar through the forfeiture of CCC loans. If this is the case and in fact it is too high, consumers are going to be paying more for their sugar than they really need to.

An additional consideration is that duties and fees tend to depress the world price of sugar. If higher fees are required because of the Initiative, the world price could be depressed further, and thereby trigger still higher fees. Thus, ironically, the Initiative could aggravate one of the main problems it is supposed to relieve—in other words, declining prices for sugar.

By depressing the price of sugar and requiring higher fees, the Initiative would be particularly damaging to the nations outside the basin from which we have traditionally imported sugar. They would experience a reduction in both volume and price. Here again, the duty rebate approach would lessen the impact of the Initiative on these other sugar exporting nations, most of whom are also friendly developing nations of strategic importance to the United States.

It might be said that if the duty rebate approach is implemented there might not be an incentive to purchase sugar from the basin. That is not the case. Because of their proximity to the United States, the basin nations already enjoy a considerable competitive advantage.

Unfortunately, the Initiative cannot operate in a vacuum. It must be tailored to the constraints of USDA's sugar program. In this regard, it will be easier for the Government to attain USDA's price objective under the rebate approach, and thereby lessen the possibility of the Government having to acquire sugar through the forfeiture of loans.

If higher fees have to be imposed, and the world price of sugar continues depressed, at some point, the Government might run out of fee authority because of the 50 percent ad valorem limit placed under section 22 fees. Under those circumstances, the Government's only alternative might be to resort to restrictive quotas on imports. Under quotas the nations of the basin might lose the special preference the Initiative is designed to grant them.

There are, of course, numerous other problems associated with quotas, and the Government has prudently refrained from employing them.

In conclusion, Mr. Chairman, we submit that the Initiative could, as it applies to sugar, generate serious problems. We believe the adoption of the duty rebate approach will improve the chances of the Initiative attaining its goals and relieve much of the anxiety over whether it will interfere with USDA's sugar program.

We respectfully urge the subcommittee to modify the program by providing for the government-to-government rebate of the import duty. Thank you.

[The prepared statement follows:]

STATEMENT OF NICHOLAS KOMINUS, ON BEHALF OF THE U.S. CANE SUGAR REFINERS' ASSOCIATION

Mr. Chairman, my name is Nicholas Kominus. I am the President of the United States Cane Sugar Refiners' Association, 1001 Connecticut Avenue, Washington, DC 20036.

Our Association represents all of the nation's independent cane sugar refiners. A list of the refiners for whom I appear is attached to this statement.

Independent cane sugar refiners are not involved in the production or processing of sugarcane or sugar beets. They refine sugar that is produced in the United States, and sugar that is imported from foreign nations.

They operate ten refineries in eight states -- Florida, Georgia Illinois, Louisiana, Massachusetts, Missouri, New York, and Texas. In addition, they operate a number of support facilities in other states.

Mr. Chairman, I appear here today to endorse the admirable goals of the President's Caribbean Basin Initiative.

In so doing, however, I must say that we believe that these goals will not be fully attained unless the structure of the program, as it applies to sugar, is modified. Indeed, as presently structured for sugar, the program could have a negative impact upon the nations of the Basin in the future.

In addition, the Initiative could, if not modified, interfere with USDA's sugar program and generate other unintended problems.

The problems involved are not insurmountable. The program can easily be modified so as to enhance its chances for success.

The Administration has recommended that sugar imported from nations in the Basin be granted duty-free status.

We recommend to the Subcommittee that it modify that proposal by providing for the collection of the duty, and for the subsequent rebating of that duty on a government-to-government basis.

The Administration has already established the precedent for this approach under the Initiative by recommending to the Subcommittee that the excise tax on rum be rebated to Puerto Rico and the Virgin Islands.

We believe that the rebate approach is far superior in that it will: first, provide the governments of the Basin with more control over economic development; second, insure that the full benefit of duty-free status is attained; third, lessen the need for even higher import fees on imported sugar, including sugar from the Basin; fourth, lessen the chance that our Government will have to acquire sugar through the forfeiture of loans under USDA's sugar program; and fifth, lessen the possibility of the Government eventually being forced into an even more restrictive program on imported sugar in order to protect USDA's program.

Under the rebate approach, the benefits of duty-free status would be received by the governments of the Basin rather than by the sugar producers. The governments can re-distribute the benefits to sugar producers and other, in a manner they believe will attain development goals.

We believe the government-to-government approach is far more appropriate, particularly because one of the goals of the Initiative is to diversify away from sugar and not to encourage more sugar production.

The Caribbean Basin Initiative is, among other things, designed to benefit the nations of the Basin by permitting them to ship certain quantities of sugar to the United States free of the import duty, which is presently 2.8125 cents a pound.

A number of nations in the Basin already enjoy duty-free status for sugar under the Generalized System of Preferences. As a practical matter, the Initiative extends this duty-free status to three other nations -- the Dominican Republic, Guatemala, and Panama. These nations do not enjoy duty-free status under GSP because the value of their sugar shipments exceeds the permitted dollar limit.

Under the tonnages involved, the total benefits of the duty-free status to these three nations would be expected to total around $71 million a year.

Based upon the experience of the past, and our expectations for the future, we believe that only part of that total will actually get to the nations it is intended to benefit.

The full benefit will undoubtedly not be attained because once duty-free status is granted the producer has an added opportunity to discount the price of the sugar he offers, if need be.

It is difficult, if not impossible, to estimate the extent of the discounting. Under certain circumstances it could, however, be substantial.

In the recent past, when the duty was just .625 cent or little more than a half cent a pound, discounting was nominal. The duty has, however, just recently been increased to the statutory maximum of 2.8125 cents or nearly 3 cents a pound.

This provides the producer with a considerable sum, and he may under certain circumstances feel compelled to negotiate away a good part of the savings in duty in order to secure a sale.

It is our understanding, for example, that Thailand's loss of duty-free status under GSP as of March 31, led to considerable discounting on its part to insure shipments.

If implemented, the Initiative will greatly expand the tonnage and the percentage of sugar that qualifies for duty-free status. As a result, it is estimated that well over half of our annual sugar import requirements could be met by duty-free sugar.

In addition to the large duty and the increased tonnage and percentage of sugar that would qualify for duty-free treatment, the situation will be further aggravated by the continuing decline in import demand. Thus, the competition among nations to ship sugar to our contracting market will intensify.

We would, therefore, expect discounting to be more of a problem in the future than it has been in the past.

Under all of these circumstances we believe that it will be difficult for the Basin nations to enjoy the full benefits of duty-free status.

The duty rebate approach would lessen the pressure to discount and increase the probability that the full benefit of duty-free status would be attained.

The Administration recognized the problem of discounting when it established the import fee on December 22, 1981. It built into its import fee structure a factor of one half cent a pound to account for discounting.

As a result, the import fee on sugar from all nations, including those in the Basin, is one half cent a pound higher than it would be if there were no GSP.

The market price, despite the imposition of large duties and fees has failed to attain the Government's price objective of 18.58 cents a pound, in good part because of the discounting under GSP.

The additional quantity of sugar that would be available for duty-free status under the Initiative might force the Administration to build even more than the present one half cent into it's fee structure.

If it does, import fees paid by all producers, including those in the Basin, would have to be higher. In this regard the Initiative would tend to be self-defeating. What's given with one hand would be partially taken back with the other.

Here again, the duty rebate approach would help by lessening the need for higher import fees.

An additional consideration is that duties and fees tend to depress the world price of sugar. If higher fees are required because of the Initiative, the world price could be depressed further, and thereby trigger still higher fees.

Thus, ironically, the Initiative could aggravate one of the main problems it is supposed to relieve -- i.e. declining prices for sugar.

By depressing the world price of sugar and requiring higher fees, the Initiative would be particularly damaging to the nations outside the Basin from which we have traditionally imported sugar. They would experience a reduction in both volume and price.

Here again, the duty rebate approach would lessen the impact of the Initiative on these other sugar exporting nations, most of whom are also friendly developing nations of strategic importance to the United States.

In the future, it might also be helpful if our Government were to extend the duty rebate approach to all GSP sugars. If the problem of discounting persists, the Government might consider reducing the duty and relying more on import fees to protect USDA's sugar program.

It might be said that if the duty rebate approach is implemented there might not be an incentive to purchase sugar from the Basin. This is not the case. Because of their proximity to the United States, the Basin nations already enjoy a considerable competitive advantage.

Unfortunately, the Initiative cannot operate in a vacuum. It must be tailored to the constraints of USDA's sugar program.

In this regard, it will be easier for the Government to attain USDA's price objective under the rebate approach, and thereby lessen the possibility of the Government having to acquire sugar through the forfeiture of loans.

If higher fees have to be imposed, and the world price of sugar continues depressed, at some point, the Government might run out of fee authority because of the 50 percent ad valorem limit that is placed under Section 22 fees.

Under those circumstances the Government's only alternative might be to resort to restrictive quotas on imports. Under quotas the nations of the Basin might lose the special preference the Initiative is designed to grant them.

There are, of course, numerous other problems associated with quotas, and the Government has prudently refrained from employing them.

In conclusion, we submit that the Initiative could, as it applies to sugar, generate serious problems.

We believe that adoption of the duty rebate approach will improve the chances of the Initiative attaining its goals, and relieve much of the anxiety over whether it will interfere with USDA's sugar program.

We respectfully urge the Subcommittee to modify the program by providing for the government-to-government rebate of the import duty.

Thank you.

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Chairman Gibbons. Thank you, Mr. Kominus. I must say that is a new approach to me. I am sure it has been tried on other people and they have had a chance to respond to it, but I will certainly give it serious consideration, and I will study your testimony and see.

One of the things that worries me is if we give a dollar-for-dollar rebate of the duty collected, wouldn't it be in the interest of those Governments down there to encourage the growing of more and more sugar when really we perhaps are trying to get them to diversify their economies?

Mr. Kominus. No, sir. I think the opposite would be the effect, because the money would not be—the benefit would not be going directly to the sugar producer.

Chairman Gibbons. It wouldn't be going to the sugar producers, but the governments might want to sell the sugar if they can get that kind of——

Mr. Kominus. I think the chances for diversifying will be much better if it is rebated to the government.

Chairman Gibbons. I agree if it is rebated to the government the chances are much better than giving it back to the producer that it would happen. But wouldn't it be in the government's self-interest if they continue to export a lot of sugar to this market? Wouldn't it almost penalize them if they didn't?

Mr. Kominus. Well, there is a limit as to the quantity of sugar they can ship to us, sir. I believe that there always is the chance that the goal of diversifying will not be attained and you would stimulate more sugar production. But I think the chances are greatly reduced under the government-to-government approach.

Chairman Gibbons. Thank you, sir.

Mr. Kominus. I might add, if I could, Mr. Chairman, that it is my understanding that the administration considered this approach and that in some parts of the administration they favor it. Apparently there were two reasons that they did not adopt it, one of which was this approach would require a budgetary line item, even though it would wash out; and the other was the Treasury's reluctance to dog-ear funds. But I think they have already set that precedent under the issuing of the rebating of the excise tax.

Chairman Gibbons. All right. Our next witness is Mr. Felipe Vicini, the chairman of the Vicini group of sugar manufacturing companies from the Dominican Republic.

STATEMENT OF FELIPE J. VICINI, CHAIRMAN, VICINI GROUP OF SUGAR MANUFACTURING COMPANIES, ON BEHALF OF THE INTERNATIONAL SUGAR POLICY COORDINATING COMMISSION OF THE DOMINICAN REPUBLIC

SUMMARY

The Dominican Republic supports the proposed Caribbean Basin Economic Recovery Act. The bill would establish an absolute duty-free annual quota of 780,000 metric tons of Dominican sugar, an amount close to the yearly level of sugar imports from the Dominican Republic in recent years. The sugar industry provides the greatest source of employment in the Dominican Republic, and plays a central role in the Dominican economy. Sugar exports account for a substantial portion of badly needed foreign exchange earnings. The proposed legislation would have no adverse effect on the U.S. price support program, because of the safeguard provisions in the bill and the basic economic factors underlying the interdependence between Caribbean Basin sugar suppliers and the United States. For the past twenty years the Dominican Republic has been the leading and most stable foreign supplier of sugar to the United States. Passage of the Caribbean Basin Economic Recovery Act would clearly promote the economic stability of the Dominican Republic and, therefore, further strengthen the friendship between the Dominican Republic and the United States.

Mr. VICINI. Thank you, Mr. Chairman and members of the committee. My name is Felipe J. Vicini. I am a private sector member of the International Sugar Policy Coordinating Commission of the Dominican Republic, a government agency comprised of both public and private sector members. I appreciate this opportunity to testify on behalf of the commission in regard to the proposed Caribbean Basin Economic Recovery Act, and in particular with respect to its provisions imposing an absolute duty-free annual quota of 780,000 metric tons for sugar imported from the Dominican Republic.

From the outset I wish to state that we support the legislation you are considering. In my country it is seen as a landmark in the evolution of the relations which should exist between industrialized and developing neighbors.

The Dominican Republic is an exporter of mostly agricultural and mineral commodities, which by and large already enter the United States duty-free. The most important exception applies to our major export item—sugar—on which presently are levied duties and import fees amounting to about 45 percent of its export price. Therefore, the provisions in the bill that would have the most immediate and meaningful impact on the economy of my country are those relating to sugar. I would like to concentrate my remarks on those provisions, after outlining the importance and the problems of the sugar industry in the Dominican Republic.

The Dominican Republic is a small tropical nation. Contrary to popular impression, climate—not land—is our primary agricultural resource. Our fundamental problem is that of using generally poor soils in ways that productively employ our population and generate badly needed foreign exchange.

Sugarcane is eminently well suited for this purpose. It is cultivated mostly in the southeastern coastal plain, in poor soils, which are not irrigated and for which the only feasible alternative is pasture for cattle grazing. Even at currently depressed sugar prices, sugarcane produces 10 times the income and employment that could be achieved from the use of these lands in cattle production.

The sugar industry is the nation's largest employer. One out of every 10 Dominicans derives his daily livelihood from the sugar industry, which includes more than 8,000 independent cane farmers.

Sugar industry exports provide upward of 35 percent of the nation's foreign exchange receipts, needed to pay for the many imported products we require, and which we cannot viably produce domestically. These include manufactured items largely imported from the United States, and virtually 100 percent of our energy requirements at OPEC prices.

Clearly, the failure of the Dominican sugar industry, for whatever reason, would impoverish our country greatly.

For the last 20 years, the Dominican Republic has been the leading and most stable foreign supplier of sugar to the United States.

Until the expiration of the U.S. Sugar Act in December 1974, we maintained a perfect record of performance in covering quotas and deficit-prorations allocated to our country. Since 1975 our yearly exports to the United States have averaged about 730,000 metric tons.

All Dominican sugar exports, about 80 percent of production, including exports to the United States, are sold under free market conditions. We are more dependent on the volatile free sugar market than any other sugar producing nation.

It is important to understand that about 80 percent of global sugar production is sold under protected or preferential marketing arrangements. This means that free market forces act only on the remaining 20 percent. For that reason, free market prices are highly sensitive to even small imbalances between world supply and demand. The result is that sugar prices in this residual market fluctuate widely.

At the present time, exporters to the free sugar market must compete with about 6 million tons of highly subsidized surpluses produced by the EEC. This figure represents over 30 percent of the volume of the free market, causing severe downward pressures on prices in that market.

U.S. sugar producers are largely insulated from these pressures because of the recent increase in the duty and the reinstatement of the variable fee on sugar imports in order to protect the price support program mandated by the Agriculture and Food Act of 1981. Because these actions tend to reduce U.S. demand for imported sugar, they also tend to aggravate the oversupply situation and further depress prices in the free market, thereby compounding our economic problems. For that reason we are heartened that the United States is considering granting an industry that is vital to the economic stability of the Dominican Republic a measure of relief from these pressures.

Section 103 of the bill would achieve that purpose without compromising the integrity of the domestic sugar price support program by placing an absolute quota on sugar imports from the three major Caribbean Basin suppliers, including the Dominican Republic. While the tariff on such imports would be removed, the import fee under section 22 of the Agricultural Adjustment Act would be retained.

We agree with the U.S. Department of Agriculture's conclusion that the sugar provisions in the bill would not undermine the U.S. sugar price support program, not only because of the safeguard provisions in the bill, but also because of certain basic economic factors.

The United States has traditionally imported 45 to 50 percent of its sugar requirements. This is not likely to change, nor is it the objective of U.S. policy to promote self-sufficiency for this commodity. Furthermore, the proximity of the Dominican Republic to the United States makes it, and other countries in the Caribbean Basin, the natural sources of imported sugar to help fill domestic demand.

Typically, Caribbean Basin suppliers account for only one-third of total U.S. imports of about 4.4 million metric tons of sugar. This would not change significantly under this bill. In fact, the 780,000 metric tons of sugar to which the Dominican Republic would be limited is close to the average annual amount we have supplied since 1975.

We believe the full benefit of the duty exemption would go to the Caribbean Basin countries as the proposal contemplates. Certainly, the Dominican producers would raise their prices by the amount of the duty reduction. In point of fact, Dominican sugar producers have inserted contingency clauses in their forward export contracts, providing that the amount of any U.S. duty exemption will be added to the price of that sugar. The acceptance of these terms by buyers in the trade reflects the basic economic factors underlying the interdependence between Caribbean Basin sugar suppliers and the United States. In this context, therefore, the interests of U.S. sugar producers under the price support program will be protected.

Mr. Chairman, I hope these observations may have helped shed some light on the salutary effect the sugar provisions in the proposed legislation would have on my country. The United States and the Dominican Republic have maintained close and friendly relations for many years. Enactment of these provisions could only strengthen that relationship.

I thank you.

Chairman GIBBONS. Thank you, sir. I don't have any questions for you right now, Mr. Vicini. I appreciate your coming.

Mr. VICINI. Yes, sir.

Chairman GIBBONS. Our next witness is from the Florida Sugar Cane League, Mr. Horace D. Godfrey.

STATEMENT OF HORACE D. GODFREY, CONSULTANT, FLORIDA SUGAR CANE LEAGUE

Mr. GODFREY. Thank you, Mr. Chairman and members of the committee. My name is Horace Godfrey, president of Godfrey Associates, Inc. I appear today on behalf of the Florida Sugar Cane League and Rio Grande Valley Sugar Cane Growers Cooperative, which represent Florida and Texas sugarcane growers and first processors. I appreciate the opportunity of being here.

I am presenting our views on the proposed CBI presented by the President to the Organization of American States on February 24 and the subsequent proposed legislation submitted to your committee.

Following President Reagan's presentation, we received many communications, both written and telephonic, inquiring as to our views on CBI. We felt it necessary, therefore, to express our views as soon as possible. This we did on March 1, 1982, by means of a letter to individuals or organizations requesting our views. I have with me a copy of this letter and it is attached to my statement, and it summarizes our views. I would like to have it included, in its entirety, in the record.

Chairman GIBBONS. Yes, sir. It certainly will be.

[The letter follows:]

EXHIBIT A

GODFREY ASSOCIATES, INC.,
Washington, D.C., March 1, 1982.

The Caribbean Basin Initiative (CBI) presented by President Reagan to the Organization of American States on February 24 included a proposed program providing for free trade of Caribbean Basin products into the United States. The only exemption was textile and apparel products.

Background information released by the White House states: "The President will request from the Congress authority to eliminate duties on all imports from the Basin except textiles and apparel. *Sugar imports will receive duty free treatment but only up to a certain limit in order to protect the U.S. domestic sugar price support program mandated by Congress.*" (Italic added)

The Agriculture and Food Act of 1981, as passed by the Congress and signed by the President, provides a price support program for domestic sugar producers and processors similar to programs for other agricultural commodities. The Administration took immediate action to implement the sugar provisions of the Act.

The CBI announcement by President Reagan is a foreign policy decision of the Administration. The Florida and Texas sugarcane producers and processors do not wish to interfere in any way with foreign policy matters; however, we strongly urge that no action be taken by the Administration or the Congress which might impede proper administration of the sugar provisions of the 1981 Farm Bill.

Enclosed is background information on the sugar program.

Sincerely,

HORACE D. GODFREY.

Mr. **GODFREY**. Briefly, we believe the CBI is a foreign policy decision of the executive branch and the Congress. The Florida and Texas sugarcane growers and processers do not wish in any way to interfere with foreign policy decisions. However, there was included in the 1981 farm bill a provision providing a price support program for sugar. We strongly urge that no action be taken by the executive branch or Congress which would prevent that program from operating and achieving the objectives set forth in the act.

Immediately upon signing the 1981 Food and Agriculture Act, the President took action to raise duties and fees on imported sugar. The Secretary established a market stabilization price which would let United States sugar flow into the market and not be acquired by the Government under the price support operation. With your permission, I submit for the record exhibit B, a brief description of the sugar program and how it works.

Chairman **GIBBONS**. We will put that in the record also.

[The exhibit follows:]

EXHIBIT B

BACKGROUND INFORMATION

The 1981 Farm Bill includes two provisions for sugar (1) a purchase program through March 1982 at a level of 16.75¢ per pound, and (2) a loan program beginning October 1, 1982, at a level of 17¢ per pound with an increase in 1982 to 17.5¢, 1983 to 17.75¢, and 1984 to 18¢.

The Administration, immediately upon Presidential signature initiated action to put the sugar provisions into effect. They are currently working on provisions to effectively implement the loan program beginning October 1, 1982.

The purchase and loan programs for sugar are similar to programs for other agricultural commodities, however, there is one big difference. Since the US must import approximately 45 percent of sugar needs, the price for imported sugar sets the price for all sugar.

Approximately 80 percent of sugar traded in world trade is done so under special arrangements or agreements. These special arrangements and agreements provide prices in some instances double the amount of the price support level included for United States sugar in the farm bill. The United States, being one of the top importers of sugar has no such arrangements or agreements. The US supplements its domestic production by importing sugar that is available after all countries having special agreements have been supplied.

There is no real world price for sugar. At times when there is a surplus of sugar in the world, over and above that traded through special agreements, the so-called world price is in reality a dumping price. When world supply is inadequate to fulfill commitments to importing countries, those countries without special agreements experience rapid world price escalation generally exceeding prices under special agreements.

Sugar provisions were included in the 1981 Farm Bill to stabilize as much as possible, sugar prices to American consumers and to maintain a domestic sugar industry. Since the United States imports about half of its sugar requirements, the price for imported sugar (which sets the price for domestic sugar) can be established at a level to insure no government sugar purchases and no sugar loan forfeitures to the government.

Section 22 of the Agricultural Adjustment Act passed in the mid-thirties provides that if the imports of any commodity is seriously impairing the operation of a domestic price support program, the President can either (1) impose fees on the imported commodity or (2) limit imports through import quotas. The Administration elected to impose fees on imported sugar in addition to duties (tariffs) to achieve a market stabilization price (domestic New York wholesale price for raw sugar with all fees and duties paid) of 19.08¢ per pound. This price, if maintained, permits domestically produced sugar to move into normal trade channels and returns to the farmer/processor (after payment of freight, storage and charges) slightly more than the 16.75¢ per pound government purchase price.

As long as sugar provisions of the 1981 Farm Bill are administered to maintain the price levels mandated in the Agriculture and Food Bill of 1981, the Florida and Texas sugar industries take no position as to the origin of imported sugar.

Mr. **Godfrey**. I must point out that imports of sugar during December 1981, in order to avoid higher duties and fees, were more than double the normal imports for December. The large tonnage of imports in December and the rush by non-GSP countries, and some countries in the process of losing their GSP designation, to move their sugar into the United States while there was a market available, has seriously impaired the operation of the program. The glut of sugar caused by these imports has kept the actual price for sugar well below the market stabilization price.

If, as proposed in the CBI, special consideration is given some countries exporting sugar to the United States, there will necessarily be reductions in sugar exported by non-GSP countries. In addition, since the United States is decreasing sugar consumption, and domestic production remains relatively stable, the overall demand for imported sugar will be reduced. These combined factors consequently indicate a strong need for the Government to closely monitor sugar imports.

Chairman **Gibbons**. In effect you say you don't like it, but you can live with it?

Mr. **Godfrey**. In effect we say it is a foreign policy matter, Mr. Chairman, and we do not want to interfere. We do want the sugar program passed by Congress last year to maintain a domestic industry and administer it in such a way as to accomplish that objective.

Chairman **Gibbons**. Mr. Bailey?

Mr. **Bailey**. I have no questions, Mr. Chairman.

Chairman **Gibbons**. Thank you, sir.

Our next witness is from the United States Council for An Open World Economy, Mr. Steinberg.

STATEMENT OF DAVID J. STEINBERG, PRESIDENT, U.S. COUNCIL FOR AN OPEN WORLD ECONOMY, INC.

SUMMARY

This testimony applauds the Administration's concern with the economic well-being and security of the countries of the Caribbean Basin, and commends the Administration for the general thrust of its Caribbean Basin Initiative (CBI). However, the trade-policy aspects of this regional strategy are less than they can and should be in both foreign-economic and domestic-economic terms. The rest of the Third World will encounter pro-Caribbean discrimination which a waiver from the General Agreement on Tariffs and Trade will not adequately assuage. The Administration's assertion that protection available against disruptive imports remains at the disposal of U.S. industry and labor is not dependable assurance that the interests of vulnerable U.S. industries, workers and communities will be adequately protected. A more far-reaching domestic-policy backstop for the CBI is needed both to ensure the effectiveness of this foreign-policy initiative and to advance the best interests of all sectors of the U.S. economy.

BOLD, BUT NOT BOLD ENOUGH

The President's commendable declaration of a U.S. initiative to help the peoples of the Caribbean Basin refers to "a crisis of unprecedented proportions." The President states that the economic well-being and security of the peoples of the area are threatened, and that "economic disaster" is threatening even the most established democracies. The United States, he asserts, is prepared "to act boldly" in responding to this emergency. However, the trade aspects (perhaps other aspects) of the CBI do not measure up to the best efforts which this description of the emergency ought to evoke. The initiative is not bold enough.

The trade-policy segment would provide duty-free, unrestricted access to the U.S. market for all Caribbean Basin exports for 12 years—with certain product exemptions or reservations: textiles and apparel, sugar, and products covered by current U.S. import-relief actions. Such concessions to Caribbean countries amount to discrimination against comparable exports from other underdeveloped countries. A waiver from the rules of the General Agreement on Tariffs and Trade would be necessary, posing problems for U.S. relations with underdeveloped countries outside the Caribbean Basin. The waiver, even if obtained, would not resolve these broader issues. The initiative the United States should be developing with respect to underdeveloped countries should encompass all such countries, many of which outside the Caribbean area are threatened with crises comparable with those in the Caribbean Basin, and merit similar boldness in our response.

The time-span of the trade concessions we provide, even for the CBI alone, should be indefinite (not limited to 12 years), subject to possible suspension, temporarily, to deal with unforeseen hardship which U.S. industries competing with these imports may encounter. The standards for suspension should be very strict.

No product should be permanently exempt. The timetable for providing free access to our domestic market might be slowed somewhat for some products in order to buy adjustment time for weak industries requiring special assistance. Such differentials in the timetable need not undermine the credibility of the U.S. initiative. Announced determination to remove import impediments on all products, with deliberate speed, would itself contribute immeasurably to the spirit and credibility of a new U.S. commitment to help the peoples of the underdeveloped countries.

One-way free trade of this scope (equivalent reciprocity cannot be expected until some distant millennium) can be made economically viable and politically palatable if it is back-stopped in our domestic policies with an adjustment, economic-development strategy that rejects simplistic recourse to import restriction and, instead, addresses the real problems and needs of vulnerable U.S. industries, workers and communities and helps them constructively, in the overall public interest over a transition period of adjustment to new realities. A full-employment policy is an essential component of such a strategy. Coherent industry-redevelopment strategies would tend to accelerate removal of any import restraints found to be essential for effective transition in industrial redevelopment.

Much more can and should be done to reassure industries, workers and communities whose products are not now exempt from the free-trade measures of the CBI policy but who fear the consequences of such access to the U.S. market. This should be done in the interests of both the Caribbean initiative and the health of the U.S. economy. The President has said: "Every protection available to U.S. industry and labor against disruptive imports will remain." The protection now available under the import-relief provisions of the Trade Act is import restriction for an entire industry that has been seriously injured by imports or is threatened with such injury, and adjustment assistance for firms, workers and communities suffering such hardship. Nor only have adjustment assistance appropriations been cut; there is no assurance of suitable job relocation for workers who have been retrained for other employment. Import restriction itself, as currently structured, has serious shortcomings as an instrument of government assistance. Firms that may not need help secure windfall gains, while firms that do need help may not receive the help they need, and may find competition from the stronger members of the industry more severe behind the new import control. The law does not require a coherent industry-redevelopment strategy as the frame-work for whatever aid is given to an industry that merits assistance. The trade legislation should be reformed to correct this shortcoming. No such reform is in the offing.

Even if an industry can make a good case for government help under the current escape clause, and the International Trade Commission recommends import restraint, there is a real possibility that the President may, at least in some cases, reject import restraint for foreign-policy reasons related to the effectiveness and credibility of the Caribbean Basin program. What if adjustment assistance to individual firms, workers and communities isn't adequate as an alternative? Is the government prepared for new initiatives in domestic adjustment? In addition to stating that every protection available to U.S. industry and labor against disruptive imports will remain, the President should have pledged government consultation with vulnerable U.S. industries, workers and communities on ways government may help forestall possible injury without suspending free access for the products involved. Alternatives to import restriction where injury has occurred or is threatened would also be explored. Reassessment of statutes and regulations materially affecting these industries, to identify and correct any inequities, is one course of action deserving attention in this regard.

Such assurances of government interest in the problems and needs of our weaker industries, and of government determination to help find solutions consistent with the total national interest, would help make the CBI policy more credible for both the Caribbean countries and for U.S. interests that may fear the policy's affects on certain sectors of the U.S. economy. The Department of Commerce should have said something along these lines in its testimony in these hearings. It did not do so.

Thus, while the Administration's concern with the economic and security problems of the Caribbean Basin is most commendable, the countries of the region have cause for apprehension over how much they will really benefit from the CBI's trade measures if success in capitalizing on these concessions leads to U.S. import restrictions to protect U.S. industries that do not effectively cope with this import expansion. Some U.S. industries, workers and communites, on the other hand, have cause for apprehension over the extent of their government's interest in the domestic dislocation that may result from these trade measures. Will some of these industries, workers and communities be sacrificed on the altar of U.S. foreign-policy imperatives in an area so near our shores and whose security is so important to our own? If import restraint is not a desirable remedy, what is and is the government prepared for it? The rest of the Third World, for its part, has cause for apprehension over the extent of U.S. interest in the well-being and security of these countries compared with the countries of the Caribbean Basin.

The CBI strategy needs to be upgraded to cover the whole Third World, to involve all the industrialized countries (thus, among other purposes, enlarging the export-market impact of expanding Caribbean and total Third World exports), and to ensure the ability of the American economy—indeed every state in the Union—to adjust most effectively to the freest access to our market for all types of Caribbean and Third World exports. The Caribbean Basin Initiative amounts to a small step in a policy area that demands but is not getting our best efforts.

Mr. **Steinberg**. Mr. Chairman, Mr. Bailey, I am David J. Steinberg, president of the U.S. Council for an Open World Economy, which is a public interest organization engaged in research and public education on the merits and the problems of achieving an open international economic system in the overall public interest. I do not speak for any private interest.

As you can see in greater detail from my prepared statement, Mr. Chairman, we believe that the Caribbean Basin Initiative is a bold effort, but not bold enough. It should go further than it does on the free trade front and further than it does regarding the domestic adjustment policy needed to back-stop such a trade policy initiative.

There should be no permanent exemptions from this free trade effort, although the time frame for applying free trade status to all products may be different for some from what it is for others.

We believe that the period should not be limited to 12 years, but should be indefinite, subject to suspensions to deal with unforeseen emergencies that may arise regarding the impact of this trade policy on domestic economic interests.

We believe also that the program should be upgraded to encompass not just the Caribbean Basin area, but all underdeveloped countries of the free world. However, the kind of domestic policy needed even to back-stop the Caribbean Basin Initiative as presently structured is not adequate.

The President has said that the procedures available to protect American labor and American industry against disruptive imports will remain. But, Mr. Chairman, this assurance is not adequate. I can envisage a situation where an industry that feels it has been seriously injured or threatened with serious injury could win a case before the International Trade Commission and then find its petition rejected by the White House because of some overriding national security interest. Surely the Caribbean Basin Initiative has a very substantial element of national security interest involved.

I can see situations, on the other hand, where American companies that may want to invest in the Caribbean area and take advantage of free trade access to the American market might hesitate because they would wonder what would happen if they should be successful in manufacturing products for export to the American market and winning substantial sectors of the American market. They might wonder, what if they were successful in this marketing undertaking; what would happen if a competing American industry should successfully argue its case in favor of import restriction. Such import restriction would certainly undermine the marketing effort that the particular investor has made.

Perhaps the most important point I can make, Mr. Chairman, in these hearings is to underscore my concern and my council's concern, free traders that we are—our concern with the serious economic problems that beset certain sectors of our economy, aggravated at this time by deep recession in our country and by substantial unemployment. I would have thought that an administration that placed so much emphasis on the importance of this Initiative, referring to the grave crisis in the Caribbean Basin area, referring to—I think these are the words the President has used—impending disaster that may be encountered by the peoples of this area—disaster perhaps now being encountered by some of the peoples of this area—that that administration would want to make sure that the Caribbean Basin Initiative gained the approval of the Congress. One way to help insure the approval of the Congress would be for the administration to show a real, serious interest in the possible problems that may arise in the weaker sectors of our society. Not only should something along these lines have appeared in the statements made by the President of the United States, but it should have appeared in the testimony by the Department of Commerce, which has a central responsibility with respect to the industrial strength of this country. Correct me if I am wrong, but I don't remember any reference to this aspect of the subject in the testimony presented in these hearings by the Department of Commerce.

I think the Government should have said it recognizes that there may be problems, there may be even serious problems. The Government should have said that it is prepared to discuss with interested industries, workers, and communities ways in which the Government might help to forestall possible injury before the possible contingency of an escape clause proceeding, with all the time that that takes and all the money that that takes these days.

So these, Mr. Chairman, are some of my reservations. I don't think I mentioned in this very brief oral summary a point I made in my prepared testimony, and that concerns feelings in sectors of the Third World outside the Caribbean area. I am not privy to what these feelings are, but there may in certain sectors of the Third World be a feeling that, although the American initiative with respect to the Caribbean is most commendable and understandable, nevertheless, for the United States to show trade discrimination in favor of the Caribbean area may suggest to some of our friends elsewhere in the Third World that the United States is less concerned with their economic problems, with the threats to their security, than with the economy and security of the Caribbean area. Therefore, I believe that a lot more thought should have gone into and ought to go into this otherwise very commendable concern by the administration with the problems of an area of the world in which we certainly ought to take a great deal of interest.

Thank you, Mr. Chairman.

Chairman GIBBONS. Thank you, sir.

Mr. BAILEY. Mr. Chairman, I just want to say that some of the comments you made concerning what happens here in the United States are appreciated. I know that the chairman has to leave, and I am very happy to address any questions later. But I appreciate that. Thank you, Mr. Chairman.

Chairman GIBBONS. Yes, thank you.

Mr. STEINBERG. Thank you.

Chairman GIBBONS. Our concluding witness today is Alfred J. Roach, who is chief executive officer of TII Industries, Inc.

Mr. Roach, as you know, we heard you recently on the trade policy of the United States, and we are glad to hear anything that you have to add.

STATEMENT OF ALFRED J. ROACH, CHIEF EXECUTIVE OFFICER, TII INDUSTRIES, INC.

Mr. ROACH. Thank you, Mr. Chairman.

My name is Alfred J. Roach. I am chairman of the board of TII Industries, Inc., which has a manufacturing plant in Toa Alta, Puerto Rico. With me is my counsel, former Congressman Jim Grover, and Fran Giambanco, my vice president of administration. Thank you for permitting my appearance on short notice to comment on the Caribbean Basin plan.

I speak as a resident of Puerto Rico and as an industrialist with deep concern for the Puerto Rican economy and the Puerto Rican worker. I realize that there are political undertones which are very sensitive to those who have intense and sincere loyalties in Puerto Rico. In no way are my comments to be interpreted as favoring any political position or faction.

As President Reagan said, "These loyal Americans have proved themselves in every war since 1898." They have fought valiantly to protect the freedoms we all hold so dear. There were more casualties per capita among Puerto Rican servicemen in Korea and Vietnam than in 48 of the 50 States. They have given their lives and their blood. We can never repay them in full measure for their sacrifices. Give them the opportunity—the economic cooperation they need to create the jobs—to earn a living.

Let me say at the outset, I support the concept of the Caribbean Basin Initiative. Surely we need a strong regional economy. Conditions in Latin America demonstrate that, certainly in Central America. But a strong, healthy Puerto Rico is the kingpin of a strong healthy Caribbean economy. Puerto Rico is the fifth best customer of the United States, with $5.6 billion imported from the United States. Puerto Rico purchases create more jobs in the U.S. mainland than their own "Operation Bootstrap" since 1956. Yet, the per capita income of Puerto Rico is one-half the mainland average.

It is said that charity begins at home and that we should have compassion for our own. But Puerto Rico doesn't want charity. The people want a fair chance to earn a wage that will provide reasonable living standards. Our first consideration in developing this legislation must be the interests of the Commonwealth of Puerto Rico.

What are the consequences of neglecting our people in the Commonwealth of Puerto Rico? A further depressed economy, more unemployment—lost markets; frustrated households and disillusioned youth. The Puerto Rican worker is skilled, dedicated, and loyal—a family man—highly motivated. With half a chance, the Puerto Rican work force will succeed even in economic adversity.

Gentlemen, without built-in protection for the Commonwealth of Puerto Rico, the low-wage rate structure in other Caribbean countries—with CBI seed money—will cause an international vacuum.

It will cause a fire storm influx of foreign capital into the Caribbean. It will light economic fires in Puerto Rico, which you and I will not put out. Don't legislate an additional burden for Puerto Rico. The present plan must have greater protection for Puerto Rico. Let us have an evenhanded Caribbean Initiative. Let us build a regional economy with Puerto Rico as a full and equal partner, a partner who will share in the benefits and help to lead in its administration; a program developed in concert with and as a consensus of the Puerto Rican people. Puerto Rico has made great strides in its "Operation Bootstrap." I know. I participated in it.

While temporarily frustrated by worldwide recession, it is working. The Caribbean Basin Initiative is a noble thought and effort; but as presently planned, it is for Puerto Rico the Caribbean Basin disincentive, with potential sociopolitical-economic shock to an already fragile economy from which there would be no free market recovery. The ultimate subsidy shoring-up by the Federal Treasury would be in the billions.

The fracturing of the Puerto Rican economy is predictable. The disaster of the 20-percent plus unemployment, industrial losses, lost markets, and opportunities are predictable. But you can't put into numbers, dollars or graphs the heartache, the personal distress, the mental anguish of parents who cannot feed their children. Deprivation and disillusionment may create even greater danger.

The economic report submitted in testimony yesterday warned of that danger:

> * * * unemployment will continue to increase, bringing with it frustration, anger, and social unrest, particularly when a whole generation of young people can find no productive activity.

May I digress, Mr. Chairman, on that whole generation of young people. Last year we witnessed, in a most law-abiding country, an explosion of youth. It was hard for our psychologists and many of our people that make those analyses to figure out what it was. I think simply they felt, and they do feel, they are left out; they have no part of what is going on in the community. If we look at our televisions at night and we see the people that are carrying the guns in the Salvadors, they don't even shave. Some of them are 12 and 14 years old. This is going on in a good part of our Western civilization.

Gentlemen, the timebomb is ticking in Puerto Rico and the United States. A great responsibility is yours. To develop an equitable plan for all the Caribbean. It will be an embarrassment to our foreign policy if our "Showcase of Democracy" in the Caribbean is no longer a shining economic example.

Thank you again for this opportunity to present my views.

Chairman GIBBONS. Thank you, Mr. Roach.

Mr. Bailey.

Mr. BAILEY. Thank you, Mr. Chairman. I want to thank you, Mr. Roach, for appearing, coming in and adding your view. You have been in business down there for quite a while. I remember you testified before the committee before in the electronics component area, I believe.

Mr. ROACH. Yes, Mr. Bailey.

Mr. BAILEY. One of the things we talked about this morning and that I am very much concerned with is the export of capital, where you have wage differentials and that sort of thing, to the point where there is a discouragement to really invest in the American, or in this case Puerto Rico and the mainland America, in their capital—especially the capital-intensive area, the high productivity capital-intensive area, as opposed some of the flexibility that we could find in the labor-intensive areas. We had this situation in New York with the cars from Japan for the MTA, where financing was a major part of the deal as opposed to quality and that sort of thing. In fact, many of the components can't even be procured in Japan, or the MTA in New York won't procure them there because they have to be serviced and repaired in this country, particularly with the drive train.

So I want to compliment you on your remarks and reflections. I have the same fears. I know the chairman is very concerned that we have a balanced policy.

That is all I have.

Mr. **Roach**. Mr. Bailey, if I may just address myself to one remark, and that was on the MTA and the cars. I asked my attorney to call the MTA, the counsel there, and ask him the one question: "Why?" And that counsel replied to him, he said: "Mr. Shariff, he said we have no choice. There are no American companies that make the cars. There are none."

Mr. Bailey, our industry has gone to Japan. Our jobs have gone to Japan. This is not just happening in the car industry. I predict—and I will give $50,000, not bet it, give it, to any charity that you name, that the price that was offered to the MTA will double in less than years, because there is a clause in the contract that says that it will escalate according to what the price of steel is. Japan has the steel.

Mr. Bailey, really, I would like—you know, it is such an important thing, the CBI, but far more important is what is happening to us in the United States in our capability to be able to manufacture, to be able to produce. We can't do it. We talked to a colonel this morning, had the same complaint. I would request Mr. Gibbons and yourself to please investigate the idea of probing. Start a congressional investigation. Let us look at what has happened over the past 5, 6, 7, 10 years. Industry has gone, jobs have gone. You will have no automobile industry in the next 3 years. You won't have it. This morning in the New York Times 45 percent more down. It is here, it is now.

I think a congressional probe is in order.

Mr. **Bailey**. Well, I know we dealt with a multitude of trade and economic issues, certainly during the discussion of the Tax Act. The chairman in fact chaired a productivity or industrial-type task force that deals specifically with this issue. So the issues are ongoing. The roots of the problems are deep. Changes and alternatives to present tax structure meet a great deal of resistance within the system, incidentally, because you are talking about huge and very rapid, in some cases, shifts in resource allocation and investment patterns in the country that alter investment patterns and investment attractiveness and things like that.

On those cars, incidentally, Japanese capacity on that portion of the contract will probably be filled, but they can produce some cars in the United States. The information we were given is not correct, I want you to know that, and for certain types of cars certainly even better cars are produced in the United States, believe it or not—certain portions of what they want to get in that contract. Ironically, a significant percentage of the components of those cars, which lends further credence to what you are saying, have to be now procured offshore. They are simply brought back in, certain things are added to them, et cetera. I was very concerned with the thing initially because of the impact on the amount of stainless steel used, about 4,000 tons, and with American unemployment in that sector at about 37 percent I was very concerned, especially since the financing package really went from the Japanese export-import bank, which is a subsidized interest bank, to the producer.

The risk is really not born by the producer over there, incidentally. That is what is ironic. The interest comes into this country at about 12½ percent, which is above the 11 percent—11.25 or whatever that is agreed on between Japan and the United States. But the Japanese company—this is the worst aspect of the whole arrangement. The Japanese company assumes absolutely no risk; that risk is assumed totally by the Government there, totally, completely.

Mr. ROACH. Absolutely.

Mr. BAILEY. And no American company would be in that position in refinancing, would be able to enjoy that advantage. So when you are talking risks of the nature that you talked about, that's where I see the fear. I happen to agree with your fears. I share them very much. But the Congress is looking. I mean I don't want to make it sound like there is a complete dearth of interest or information here, because there really is not. There is a great deal of interest and discussion on these issues. I just happen to be one who concentrates on it a great deal.

Mr. ROACH. Congressman Bailey and Congressman Gibbons, if I may, I know of your great war records and the great sacrifices you have personally made for this country, and what you are doing now, too. I look at the Members of Congress, frankly, and my heart bleeds for you, because I see people out in our economy, ballplayers, comedians, songwriters, and tap dancers, that earn $500,000, $600,000, and $1 million. Coming down on the plane I was talking to Jim about it, and I said how many constituents does a Congressman represent? He said 500,000. I said that's less than 10 cents apiece. Don't you think they are worth more than a dime? Why don't we give them $1 apiece.

Mr. BAILEY. Geez, I like this testimony all the better. This is sounding great to me, I'll tell you.

Mr. ROACH. I mean that sincerely. I mean that sincerely. And I will speak out on it. I think it is ridiculous what we are doing. I have seen so much of this stuff going on in the papers, how bad and how shortcoming and so forth it is. I think it is the most patriotic group that we have in the country. And I want to tell you that I am grateful for it, and I want to thank you for your services. And I know the time—because I have men working for me, former Congressman Jack Wydler and Jim Grover—the time that you stay away from your families. There is no way that people can pay for that. And yet you are vilified in the press, and I think it is terrible.

I would like to associate myself with the remarks and say thank you for the people I know and for my family for what you are doing.

Mr. BAILEY. I won't argue with you.

Mr. ROACH. And I still say I would like to have a probe of where our jobs have gone. How are you going to face your constituents when they look at you and say Congressmen Bailey and Gibbons, where are the jobs? The Government can't give jobs. The Government administrates for us. It is the manufacturers that give the jobs. We have to produce the income. We need the cooperation of the Government. I don't want you to do my job. We will do our job.

Mr. BAILEY. I know the chairman has to go. I would just add to that that I hope in looking at those problems that we do understand that the wealth—all wealth eventually, everything that we do, all the technology we have merely represents an accumulation over countless years of the investment of labor, technology, sweat, and toil. And everything begins with the conversion of raw materials and capital goods, and that all those goods and services that we talk about trading and dealing with float on that bed of basic productive production, capital-intensive industries that really provide the roots of wealth, material wealth for the entire society. It all comes from there. It has to begin somewhere with some mineral, some raw form of energy, some labor input. It represents a history of technology and investment. That is where it all starts, and the Nation's security is very much tied to that base, and I thank you for your reflections, because I happen to believe it is vital to our well-being.

Mr. ROACH. Thank you. I might address the Chair and state I have the great privilege and honor of meeting tonight at 5 o'clock with the Vice President of the United States to express some of my views and some information that I have gathered that he is interested in. And I believe you will hear more from that. And I will keep this committee informed, if I may, of what I think can and should be done. Thank you, gentlemen.

Chairman GIBBONS. We are glad to have your views. Mr. Frenzel.

Mr. FRENZEL. No questions.

Mr. ROACH. Thank you, sir.

Chairman GIBBONS. When you see the Vice President, tell him hello. He used to be a member of this committee, and we remember him fondly.

I don't want anybody to think I am making a pro-Japanese statement now, but I was just looking at the figures that were published by the Department of Commerce, and they show that over the last 10 years, 11 years, the Japanese share of world trade has increased by 1.5 percent and the U.S. share of world trade has decreased by 2.2 percent—of exports we are talking about now. And I notice also that France, Germany, and the United Kingdom have all lost a share of world trade. So it means that it wasn't really—we didn't lose all of our trade advantages to the Japanese. We lost them to other developing nations. Now world trade, of course, is far larger. It is about 10 times larger now than it was 10 years ago. It has gone up very dramatically.

But I am not sure what all these figures prove. I guess it all depends upon how you look at them. When you are talking about why the difference in the pay of entertainers and the pay of Congressmen, I would say that looking at it from another point of view, America is more interested in improving the quality of its entertainment than it is in improving the quality of its government. Maybe that is where the problem lies.

Mr. ROACH. Maybe they need somebody like me to start to speak out. And I will. I promise you that. By the way, on figures of economists, it reminds me of the soothsayers of the pharaohs. I don't put too much stock or too much money in what they say, respectfully.

Chairman GIBBONS. We appreciate your coming and taking the time. We know you have been very patient in waiting. This concludes the hearings of the Trade Subcommittee on the Caribbean Basin Initiative proposed by President Reagan. The subcommittee has received a great deal of useful information and views from more than 45 witnesses. These views and proposals will be considered carefully by the subcommittee in its future work on this program.

The formal record of these hearings will remain open until the close of business on Thursday, April 1, for inclusion of additional written statements and materials. The subcommittee is adjourned until further call of the chair.

Thank you very much.

[Whereupon, at 2:30 p.m., the hearing was adjourned.]

[The following material was submitted for the record:]

AAMA

March 19, 1982

RECEIVED
MAR 22 1982
Ways and Means
Subcommittee on Trade

Hon. Sam M. Gibbons, Chairman
Subcommittee on Trade
House Committee on Ways and Means
233 Cannon House Office Building
Washington, D.C. 20515

Dear Mr. Chairman:

Attached is a statement of the American Apparel Manufacturers Association (AAMA) on the Administration's proposed Caribbean Basin Initiative which we would appreciate being included in the record of hearings on this subject.

AAMA is the central trade association of the U.S. apparel industry representing companies that account for about two-thirds of domestic capacity for manufacturing apparel. Our membership embraces firms in every line of apparel production.

Generally, our statement endorses the Initiative but makes specific recommendations as to its implementation with regard to apparel trade.

Sincerely,

Ellis E. Meredith

Ellis E. Meredith
President

EEM:bal

Attachment

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1981–82

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†Past Chairman
***Honorary AAMA Board Member**

The American Apparel Manufacturers Association's Position on The Administration's Proposed Caribbean Basin Initiative (CBI)

The Administration is developing a new and comprehensive trade and investment policy to assist the nations of the Caribbean Basin in their economic development. The general elements of such a policy already have been outlined. This paper submits the views of the American Apparel Manufacturers Association on the CBI.

The apparel industry recognizes the political and economic importance of the area to the United States. It also has a large stake in the development and stability of the region. Traditionally, it has been of special interest to the United States, and should continue to receive this country's priority attention in its economic and political development.

Our industry supports and encourages the President's initiative regarding the nations of the Caribbean Basin.

The apparel industry can make a major contribution to the benefit of these countries. Ours is still a relatively labor intensive industry which can put a very large number of people to work quickly. Training of local management and workers can be accomplished in much shorter time-spans than in other industries, and with relatively less capital requirements. Several American companies already have operations in the area and can supply the technical, training, and marketing assistance required to initiate or enhance local production. In several ways the technical and human resources the apparel industry can provide toward development in the caribbean will have greater long term benefits than simplistic financial aid or expenditures for large scale capital projects.

As we understand the proposed arrangement, bilateral apparel and textile trade agreements under the Multifiber Arrangement (MFA) would not be disturbed by the CBI. According to information presented to the industry's trade sector advisory committee: "All products, excluding textiles, from countries designated as beneficiaries of the arrangement would be imported free of custom duties. Consistent with our textile policy of limiting growth under large quotas from our major suppliers while providing more favorable access for small and new suppliers, we will seek to provide increased access for Caribbean exports of textiles and apparel. This increased access will be related to our ability to tighten up on the access provided to our major suppliers and the implementation of these policies will develop in parallel."

We welcome this position. Not only does it take into account established policy with respect to international trade in apparel and textiles, it also recognizes the need for a global strategy to meet the ongoing import problem confronting this industry.

In this connection, we offer the following recommendations which, with respect to the apparel industry, we consider essential to the effective implementation of any Caribbean Basin Initiative:

1/ U.S. imports of apparel from Caribbean Basin countries must be governed by the terms of the MFA. The recently negotiated protocol extending that instrument provides for differential treatment of large, more developed exporters of apparel as opposed to developing and less developed suppliers. However, it does not contemplate the growth of such imports from developing countries in such volume as to create or contribute to market disruption already present in the United States.

Recognizing the severity of the apparel/textile import problem and the economic significance of the domestic industry, President Reagan, as a candidate, wrote Senator Strom Thurmond on September 3, 1980 that:

> "The MFA...needs to be strengthened by relating import growth from all sources to domestic market growth."

This position was firmly restated on December 11, 1981 by James A. Baker III, the President's Chief of Staff, who wrote Senator Thurmond and Representative Carroll A. Campbell:

> "In follow-up to our recent conversations, I want to emphasize the importance that President Reagan attaches to the textile import question. In this regard, and in view of the current situation in the domestic market, the President has instructed the U.S. negotiators in Geneva to strengthen the U.S. proposal presented in Geneva on the renewal of the MFA.
>
> "This Administration will make every effort to satisfactorily conclude an MFA that will allow us to relate total import growth to the growth in the domestic textile and apparel market. The President has authorized me to reaffirm that we shall work to achieve that goal."

In introducing the United States protocol for extending the MFA in the GATT Textiles Committee on September 21, 1981, Chief Textile Negotiator Peter Murphy said:

> "The basic situation as we see it, Mr. Chairman, is that the next few years will be difficult ones indeed for world trade in textiles. All of the conditions which led to conclusion of the original MFA are still with us, and the situation is further aggravated by basic and persistent economic problems affecting the economic growth and employment patterns of most developed countries.

> "In the case of the United States, Mr. Chairman, we foresee very low rates of growth in domestic consumption of most textile products over the foreseeable future. This means, Mr. Chairman, that in the United States we are going to have to pay particular attention to the rate of growth of imports to domestic market growth, particularly in product areas which are already heavily impacted.
>
> "We now have instances of severe market disruption in certain products in the United States. In the case of major suppliers of these products, we will not be able to offer the same rates of growth and flexibility as in the past. We do also assert, however, that we would continue in the future, as we have in the past, to agree to at least Annex B levels for those suppliers not contributing to complex market disruption.
>
> "So where does this leave us, Mr. Chairman? We believe it [the U.S. protocol] leaves us with an MFA interpreted to meet this situation. The MFA clearly provides in paragraphs 2, 3 and 5 of Annex B for lower rates of growth and flexibility in exceptional cases and circumstances.
>
> "The MFA in Article 6 and elsewhere makes clear the concept that more favorable treatment should be accorded new entrants and small suppliers. We believe this is a particularly important element of the MFA. We have already gone to considerable lengths to follow this percept in the past with regard to both growth and flexibility and we will make every effort to do so in the future. The degree of our ability to meet these goals with respect to certain sensitive products will depend, however, on our ability to deal successfully with imports from larger suppliers of the same products."

And in his closing statement to the Committee on December 22, 1981, Mr. Murphy said:

> "We believe the provisions of this protocol will be sufficient for the United States to address its concerns, particularly with respect to participants accounting for a very large share of the U.S. import market. Any bilateral solutions must be both pragmatic and equitable."

In any Caribbean Basin initiative, the U.S. apparel industry must insist that the growth of imports from such countries and the flexibility provided them in bilateral agreements not exceed the levels stated in Annex B of the MFA. Secondly, Annex B treatment of Caribbean Basin nations must be contingent upon limiting the growth and flexibility of large suppliers. Third, we strongly recommend that in addition to lower growth and flexibility, every effort be made to restrain the trade of large suppliers to permit a more equitable sharing in our market by both the U.S. industry and that of Caribbean Basin countries. Finally, sensitive categories of apparel already heavily impacted by imports should not receive more favorable MFA treatment.

2/ Rules of origin must be carefully drawn and strictly enforced if Caribbean nations are to develop economically sound industries and if problems of transshipments are to be avoided. The new protocol extending the MFA provides adequate tools to meet this problem, and we recommend that an appropriate visa system (patterned after that established by the Dominican Republic) be included in any apparel/textile bilateral agreement negotiated with any of the Caribbean countries.

3/ The Subsidies Code recently concluded as part of the Tokyo Round of the Multinational Trade Negotiations must be strictly enforced and appropriate safeguards against subsidized exports from Caribbean nations applied.

4/ As the CBI is implemented and the economic development of the Basin countries proceeds, trade must and will eventually become two-way. To capitalize on the opportunities that undoubtedly will emerge, we recommend that the Administration redouble its support of Export Trading Company legislation currently pending in the Congress. This measure will provide small and medium size companies a means to expand trade between the United States and the Caribbean Basin.

5/ Because of their relationship with the United States, we suggest that special treatment, in certain circumstances, be considered for Puerto Rico and the Virgin Islands. The conomic development of these islands cannot be jeopardized as we help their neighbors. Specifically, and with particular regard to Puerto Rico, we recommend that administrative action be taken through the application of appropriate "safe-haven" rules to assure the economical operation of apparel manufacturing on the island.

Our recommendations are designed to accommodate a major new national trade and economic development initiative with long standing policy respecting the U.S. apparel and textile industry. We believe it to be fair, achievable and consistent with the President's stated objectives. We anticipate working closely with the Administration and the Congress in the development and application of the Caribbean Basin Initiative.

We have a national obligation to help foster economic and stable political development in the Basin. We also have a compelling obligation to preserve our domestic industry. Working with our government, we believe a policy that will meet all of our objectives can be achieved.

STATEMENT OF CHEMTEX, INC.

SUMMARY

Chemtex, Incorporated supports H.R. 5900, the Caribbean Basin Economic Recovery Act, and suggests that the legislative history clarify the intent of § 103(b) of the bill, which excludes from duty-free treatment "textile and apparel articles which are subject to textile agreements." Since the statutory language is identical to § 503(C)(1)(A) of the Trade Act of 1974, the textile exclusion for the Generalized System of Preferences (GSP) program, the language should be interpreted and administered in the same fashion, i.e., excluding from duty-free treatment only those textile and apparel items which are actually subject to quantitative restrictions under the Multi-Fiber Arrangement (MFA).

STATEMENT

Chemtex, Incorporated is a domestic corporation engaged in the design, engineering, erection and operation of plants to produce man-made fibers and films, covering textile filament and staple, fibers for industrial and home uses, and miscellaneous specialty items. Chemtex' ownership interest in numerous production plants around the world provides for continuing technical developments, in-plant training facilities, and a pool of experts readily available for new plant start-ups.

In 1974, Chemtex entered into a joint venture arrangement with Olympic Fibers in Costa Rica, for the production of "pre-oriented polyester filament yarn" (POY), which is sold as a continuous filament item.

POY is produced from small polyester chips (purchased from the United States, and representing approximately 50% of the final sales price of the POY) which are specially treated and then fed into a spinning system, where the chips are melted in an electrically heated extruder, filtered, and then pumped through a number of dies, producing fine strands (filaments) that are quenched by a cross flow of cool air, collected into bundles of filaments, coated with a special protective lubricant, and wound up on spools.

In its finished form, POY is purchased by customers in North and South America, who use it to produce a wide variety of end products, primarily apparel (trousers, suits, shirts, blouses, rainwear, and sweaters) and home furnishings (sheets, pillowcases, and tablecloths).

The Caribbean Basin Economic Recovery Act, which proposes to establish a "one way free trade zone" between the United States and eligible countries (including Costa Rica) presents a unique opportunity for the United States to fashion a beneficial trade arrangement with Central American and Caribbean countries without a large revenue or trade impact. For example, the elimination of U.S. duty on POY from Costa Rica would not have any significant adverse impact on the U.S. Treasury -- if Olympic Fibers were to sell in the U.S. twenty-five percent (25%) of its total POY production and all U.S. duties were eliminated on that product, the cost to the U.S. Treasury would be less than $500,000 per year. Moreover, Olympic Fibers is the only producer of POY from all the countries which are eligible for preferential treatment under the Caribbean Basin Initiative. Obviously, U.S. imports of POY from other areas outside the scope of the Caribbean area would not be affected, thus precluding a sudden surge of duty-free imports on a world-wide basis.

It is important to note that POY (classified under TSUS 309.31) is not subject to any bilateral textile restraint agreement under the Multifiber Arrangement (MFA). While there are two bilateral textile agreements between the United States and Costa Rica, both due to expire at the end of 1983, neither agreement covers POY. The limitations of the first agreement pertain to trade in textile category 649 (man-made fiber, brassieres and other body-supporting garments); the other agreement establishes a consultative mechanism concerning trade in other textile product categories. Moreover, no bilateral agreement from any other country restrains trade in POY. At the present time, however, the existing 10.5% duty does constitute a barrier which prevents Olympic Fibers from selling large volumes in the U.S. market.

Even with the duty-free treatment provided by the Caribbean Basin Initiative, Olympic Fibers anticipates that it could export a maximum of 25% of its total capacity to the U.S., or about 3.46 million pounds per year. This figure represents 0.2% (2/10 of 1%) of the total estimated 1981 U.S. filament capacity (1.6 billion pounds) -- hardly a significant market share. Moreover, the Caribbean Basin legislation contains a number of safeguard mechanisms such as the minimum content requirement and the ability to use the remedies available under sections 201 to 203 of the Trade Act of 1974, should a threat of injury or injury itself actually develop in a U.S. industry, because of the duty-free imports.

There is one important point of clarification which Chemtex suggests be added either in the legislation or the legislative history. This concerns the interpretation of section 103(b) of the bill, which states in full that "the duty-free treatment provided under this title shall not apply to textile and apparel articles which are subject to textile agreements." The section-by-section analysis of the bill which the Administration prepared does not explain the intended application of this provision, nor does the

White House February 24 "Fact Sheet" on Caribbean Basin Policy.

It is the position of Chemtex that section 103(b) be interpreted in the same manner as the identical language is interpreted for purposes of the Generalized System of Preferences (GSP) program, i.e., excluding from the category of eligible articles only those textile and apparel articles which are presently covered under a restraint agreement pursuant to the MFA, and not covering items like POY, which are not subject to any such quantitative restraint. We believe that this is the proper interpretation of the legislation as it is now written. President Reagan, in his speech to the Organization of American States on February 24, stated:

> The only exception to the free trade concept will be textile and apparel products because these products are governed by other international agreements. However, we will make sure that our immediate neighbors have more liberal quota arrangements.

The clear implication, thus, is that the textile exclusion is limited to those articles already subject to some kind of MFA quota. POY is not subject to any such quantitative restriction. The logic of applying a more generous quota for the textile products excluded form the CBI's duty-free treatment necessarily assumes that some type of quota is already in existence. This interpretation is reinforced in a statement made by Ambassador Brock during the course of the briefing for reporters, also held on February 24th:

> Secondly, the trade area, there is one exception which I think, is fairly obvious and that's in the textile and apparel area simply because it's covered by the international agreement, the Multi-Fiber Agreement . . . (emphasis added)

Moreover, the language of § 103(b) is identical to the textile exemption from the Generalized System of Preferences (GSP) program, contained in § 503(C)(1)(A) of the Trade Act of 1974. The established interpretation of the GSP textile exemption is that it applies only to articles actually subject to a quantitative restraint; thus, a significant number of textile and apparel items classified in Schedule Three of the U.S. Tariff Schedules ("Textile Fibers and Textile Products") are presently GSP eligible items. It would certainly appear that, in adopting the identical language, the Administration should administer the textile exemption in the same manner for purposes of the Caribbean Basin Initiative. Any other interpretation would lead to the anomolous result whereby identical statutory language would be administered differently for the two programs; there is simply no valid legal justification for such an outcome.

As President Reagan noted in his February 24 speech to the Organization of American States, the Caribbean Basin Initiative is designed to create conditions under which creativity, private entrepreneurship and self-help can flourish. Olympic Fibers is a highly visible, high-technology plant which is vital to the Costa Rican economy. Since Olympic Fibers is also one of the most significant and technologically advanced employers in the country, the elimination of U.S. duties on POY would increase the training and employment opportunities for Costa Rican laborers, and increase hard currency revenues to the government.

For a country like Costa Rica, whose foreign debt is nearly $3 billion, the CBI offers hope for overcoming the problems associated with massive debts and capital flight. Moreover, Ambassador Robert J. Ryan, the State Department coordinator for the Caribbean Basin Initiative, testified before the Trade Subcommittee that Costa Rica is a country with a strong democratic tradition which could be a model for the rest of the region if it could resolve its economic problems; the CBI represents a foundation upon which economic development may prosper. This unique opportunity must not be hampered by unnecessary restrictions and disincentives.

STATEMENT OF ROBERT AUERBACH, GENERAL COUNSEL, CYCLE PARTS AND ACCESSORIES ASSOCIATION, INC.

SUMMARY OF RECOMMENDATIONS

I. Provide a specific exemption for bicycle components in view of their import sensitivity; alternatively, provide an administrative procedure whereby industries such as ours may seek relief upon a showing of injury.

II. The Caribbean Basin Initiative should contain rigid guidelines as to when a product will be considered "made" in the beneficiary nation in order to avoid the abuses stemming from the practice known as "transhipment."

III. The Caribbean Basin Initiative should provide a cutoff of benefits to any beneficiary nation which commits an unfair trade practice.

* * *

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The Cycle Parts and Accessories Association is comprised in membership of the leading domestic manufacturers of bicycle components. Although this organization strongly supports the intent behind the Caribbean Basin Initiative, several aspects of the program may have the unfortunate consequence of causing serious economic injury and loss of employment to the members of our organization. Accordingly, we are filing this written statement and ask that it be made part of the formal record so that the Subcommittee on Trade shall be aware of our concerns and, hopefully, adopt appropriate measures to alleviate them.

Despite technological advances, the production of bicycle components remains, essentially, a labor intensive activity. Countries with labor cost advantages do exceptionally well in our market. During the 1950's, our primary foreign competition came from Western Europe. In the 1970's, Japan exploited her comparative wage advantage and became a formidable competitor, and it remains so today.

By the mid 1970's, such developing countries as Taiwan and Korea emerged as important suppliers to this market. Japanese capital and technological know-how often played a role in their initial successes. Later, they were joined by Singapore, India and other developing countries. Thus, it is clearly evident that developing countries with low cost labor offer very attractive locations for the production of bicycle components. Our country has been perhaps the most generous of all in terms of accepting the output of these countries.

In 1981, imports of bicycle components exceeded two-hundred million dollars and a good portion of this came from the developing countries.

Imports now command a 60% share of our market and our "import sensitivity" has become an accepted fact.

Taiwan, Korea, Singapore and India have all made strong inroads in our market despite the current tariff rate on bicycle parts and the high shipping costs they must bear. One shudders to think of the consequences of the Caribbean Basin Initiative which will encourage production in low labor cost countries right on our doorstep. With the advantage of no tariff, and without the disadvantage of high shipping costs, these Caribbean Basin countries could literally innundate our market with their products, and, in the process, drive many domestic producers out of business.

For all of these reasons, we urge the Committee to carve out a special exemption for bicycle components, just as it has done for textile and apparel. Alternatively, we ask that the final legislation include an administrative procedure whereby import sensitive industries might seek some relief upon a showing of injury. To our knowledge, the present legislative package includes no such administrative procedure.

We would also like to bring to this Committee's attention another problem which the Caribbean Basin Initiative does not seem to address. This problem, namely, transhipment, has probably been brought to your attention in connection with the Generalized System of Preferences. It is a practice whereby goods from a non GSP nation are transhipped to a GSP nation and ultimately end up in this country free of duty. Our government has had some success in eliminating this abuse, yet we understand that the practice continues.

Fortunately, there are ways to discourage this abusive practice.

One way is for the Caribbean Basin Initiative to provide specific guidelines as to when a product will be considered "made" in the beneficiary nation. A substantial addition to the value of the final product should occur there. Otherwise, you can be sure that the Caribbean Basin Initiative will be abused with foreign producers transhipping their merchandise to a Caribbean nation enroute to the United States with only a minor manufacturing step occurring in that nation. Strong requirements are needed in this sensitive area to ensure that the benefits flow to the Caribbean Basin nation and not to a producer elsewhere.

Finally, we strongly urge the Committee to include sanctions, such as the elimination of benefits, in cases where the Caribbean nation commits an unfair trade practice. Specifically, we are referring to direct government subsidies of domestic production, a common phenomena in economies where there is a substantial measure of central control, such as exists in the Caribbean Basin. Also, the legislative package should incorporate swift and strong sanctions to deal with the dumping of merchandise in this country at less than fair value.

At this very time, two members of this organization are vigorously pursuing antidumping and countervailing duty remedies with respect to imported tires and tubes and bicycle speedometers. Further initiatives for other bicycle components are under consideration. The Caribbean Basin nations must be made to understand that these practices will not be condoned by our country and will result in an immediate cutoff of benefits under the program.

The Cycle Parts and Accessories Association appreciates this opportunity to submit this written statement and we stand prepared to furnish whatever other information the Committee may request.

STATEMENT OF JOHN HIMMELBERG, ON BEHALF OF THE FLORIDA TOMATO EXCHANGE, ORLANDO, FLA.

INTRODUCTION

Mr. Chairman, thank you for giving me the opportunity to share the views of the Florida Tomato Exchange ("Exchange") with this Committee. My name is John Himmelberg and I am an attorney with the law firm of Barnett & Alagia in Washington, D.C. and Palm Beach, Florida. I am authorized to present the Exchange's views before this Committee.

The Florida Tomato Exchange is a non-profit cooperative, agricultural association whose members represent approximately 80% of the volume of fresh tomatoes shipped from the State of Florida. For your information, the Florida tomato industry shipped in excess $244 million dollars worth of tomatoes out of Florida last season which represents more than one third of the total value of all fresh vegetables produced in Florida. The

Florida tomato industry alone provides jobs for more than seven thousand workers, many of whom are not qualified for other employment due to their education and background.

The Florida Tomato Industry at one time provided nearly all the tomatoes consumed in the United States during the winter months. However, a large part of the market was lost to imports from Cuba; and, since trade relations with that country terminated in 1960, Mexican imports of tomatoes and other winter vegetables have plagued, and now seriously jeopardize, the future of Florida's largest vegetable industry.

The Florida Tomato Industry has taken meaningful steps to regulate unfair domestic practices by adopting a federal marketing order and by organizing the Florida Tomato Exchange. These efforts, however, have been and continue to be seriously undercut due to preferential treatment of imports by the United States government.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

The Exchange is concerned that the Caribbean Basin Initiative ("CBI") artificially creates an atmosphere conducive to raising imports to the United States of perishable agricultural products which directly compete with U.S. and, in particular, Florida producers. In addition, the CBI's provision for protecting the U.S. perishable agricultural producers simply is too burdensome and time consuming to offer any real relief or protection. Significantly, the CBI fails to guarantee that the peoples of the beneficiary countries are the real recipients of the U.S. largess. Additional problems of assuring favored treatment only to the designated CBI countries, pest and pesticide problems which exist in the CBI countries are dealt with, if at all, only in a cursory and ineffectual fashion.

Accordingly, for the foregoing reasons and the reasons stated below, the Exchange must oppose the CBI as proposed as it pertains to perishable agricultural commodities.

In the short term, the CBI cannot accomplish what it proposes to do through free trade. And, it is questionable that the CBI can accomplish its goals in the long term. When viewed against the potential harm to Florida agriculture and labor which impact has not been mentioned or assessed, the CBI must be challenged.

The Exchange requests that the CBI legislation be amended to prevent tomatoes and all other perishable agricultural commodities from being added to the GSP list.

However, if the CBI is enacted, we recommend that Congress assure that: 1) U.S. aid reaches those for whom it is intended; 2) products granted duty-free status actually are produced, substantially manufactured, or assembled in the beneficiary countries, 3) workable and effective safeguards are enacted to protect U.S. producers of competitive perishable agricultural commodities; 4) goods from ineligible countries are not qualified for duty free treatment by shipping them through beneficiary countries; and, 5) every step possible is taken to prevent pests such as the fruit fly from entering the United States.

ONE-WAY FREE TRADE

The centerpiece of the U.S. program is the offer of one-way free trade of all products into the U.S. market even though currently the countries of the region are already afforded liberal entry into the United States. Accordingly, the Administration announced that the President will request from the Congress authority to eliminate duties on all imports from the Basin except textiles and apparel.

The Administration indicates safeguard mechanisms will be available to any U.S. industry seriously injured by increased

Basin imports and that rules of origin will be liberal to encourage investment but will require a minimum amount of local content (25%).

The President will also seek congressional authorization to grant tax incentives to U.S investors in the Caribbean Basin and will request supplemental assistance appropriations of $350 million in fiscal year 1982.

The Administration indicates it will seek legislative authority to grant beneficiaries in the Caribbean Basin duty-free treatment for twelve years for all products except textiles and apparel items which are subject to textile agreements. The safeguard mechanism proposed requires a finding by the International Trade Commission that increased imports are a substantial cause of serious injury or threat thereof to U.S. domestic industry and a recommendation to the President to grant relief. For perishable commodities, the legislation provides authority for the Secretary of Agriculture to recommend to the President the restoration of most-favored-nation (MFN) treatment on an immediate basis if warranted pending the completion of the formal escape-clause process.

The rules of origin under the free trade arrangement are an important factor in determining the accessibility of duty-free access for resource-poor Basin countries. The Administration indicates that the free trade area has been designed to avoid fostering the type of investment in the region which would result in mere "pass-through" operations involving little value added in the country.

With regard to the Generalized System of Preferences (GSP), the Administration believes GSP has a complex structure which limits the ability of small and relatively inexperienced countries such as those found in the Caribbean Basin. Also, the Administration believes that many of the more promising prospects for Basin exports are in categories which have been excluded legislatively from the GSP program for global reasons which are not relevant to Caribbean Basin. Also, the Administration believes that the GSP has both dollar and percentage limitations which are arbitrary in their application to many Caribbean Basin products. These are the principal reasons why the Administration seeks one-way duty free trade for the Caribbean Basin countries.

Stripped of the rhetoric, the CBI, as it pertains to perishable agricultural commodities, represents a dramatic departure from the Trade Act of 1974. Congress should be wary of this proposal and consider carefully its ramifications.

GSP tariff preference programs currently in place are designed to help developing countries increase their exports, diversify their economies and lessen their dependence on foreign aid. The GSP schemes are generally similar in terms of product coverage and the number of developing countries eligible to receive benefits. All programs include safeguard limitations designed to protect sensitive domestic industries and to ensure that benefits are extended to less competitive beneficiaries.

The U.S. GSP is administered in accordance with Title V of the Trade Act of 1974 which sets out the criteria for determining GSP country and product eligibility for limiting preferential treatment. The initial list of GSP eligible items was formulated following public hearings by the U.S. International Trade Commission and the U.S. Trade Representative's Inter Agency Trade Policy Staff Committee. Regulations governing the GSP provide for an annual product review during which interested parties can petition for modifications to the GSP product list. While the program is designed to encourage the expansion of developing countries' exports, careful consideration is given to the impact on domestic interest before products are designated for GSP duty free treatment.

The competitive needs exclusion set out in Title V provides further assurance that GSP duty free imports do not adversely affect domestic industries. Less than two years ago, the prior Administration found that the GSP program "...has provided important increased opportunities for developing countries to diversify and expand their exports." Report to Congress on the First Five Years' Operation of the U.S. Generalized System of Preferences (GSP), Transmitted by the President of the United States on April 17, 1980, Committee on Ways and Means, U.S. House of Representatives, WMCP: 96-58, p. IX.

Moreover, under present law, in providing duty-free treatment for eligible products from developing countries, the President is required to take into account: 1) the effect such action will have on furthering the economic development of developing countries; 2) the extent to which other major developed countries are undertaking a comparable effort to assist developing countries by granting generalized preferences with respect to imports of products of such countries; and 3) the anticipated impact of such action on U.S. producers of like or directly competitive products. 19 USC §2461.

The CBI presents no good reason why these criteria suddenly should be dropped.

The regulations implementing the administration of GSP provide that any interested party may petition to have new articles added to the GSP list. Petitioners are responsible for providing detailed economic analysis to support the request and are required to include information on U.S. and developing country production, employment, cost and profits. Petitions are reviewed by the Trade Policy Subcommittee which receives legally required advice from the U.S. International Trade Commission, the views of all interested parties and background studies prepared by individual member agencies of the Trade Policy Subcommittee. The import sensitivity of the item in the context of the GSP is also carefully evaluated. Again, the Exchange wonders: Why change this process now, which obviously has been considered carefully.

Over the past several years petitions to add items to the GSP have been denied because agency background studies and testimony from domestic producers indicated that elimination of the tariff on imports of these items from beneficiaries could lead to increased imports which would adversely affect U.S. agricultural producers because beneficiaries already had demonstrated their ability to compete in these items on a Most-Favored-Nation basis.

The present U.S. program is designed to ensure that imports of GSP duty-free products do not affect adversely U.S. producers of competitive items. As in the case with the preference schemes of other donor countries, the U.S. scheme excludes certain categories of import-sensitive goods from duty-free treatment. And, special consideration is given to the extent to which these items are import-sensitive in the context of the GSP. Accordingly, it appears that the existing GSP review procedures and provisions have offered increased opportunities for developing countries to expand their exports while at the same time they have been successful in safeguarding the interest of U.S. producers and workers. The CBI proposes to grant duty-free treatment without any justification and without any consideration of the impact on domestic industry.

In summary, the proposed CBI overrules outright part of the 1974 Trade Act and its implementing regulations and specifically ignores the anti-competitive effect of perishable agricultural imports from the Caribbean Basin on Florida and U.S. agriculture and workers.

TRADE ACT OF 1974

The principal purposes of the Trade Act of 1974 are:

> To foster the economic growth of and full employment in the United States and to strengthen economic relations

> between the United States and foreign countries through open and non-discriminatory world trade;
>
> To establish fairness and equity in international trading relations;
>
> To harmonize, reduce, and eliminate barriers to trade on a basis which assures substantially equivalent competitive opportunities for commerce of the United States; and
>
> To provide adequate procedures to safeguard American industry and labor against unfair and injurious import competition.

In one fell swoop, the CBI dramatically alters these principles with regard to perishable agricultural products. By design, the CBI establishes unfairness and inequity in international trading relations with the Caribbean Basin countries. No mention has been made of the trade restrictions imposed by Caribbean Basin countries on U.S. produce. Shouldn't the Committee know that such restrictions exist and are substantial?

By design, the CBI assures substantially inequivalent competitive opportunities for commerce of the United States. And, the CBI's safeguard procedures are simply a case of too little too late with respect to perishable agricultural commodities.

The Administration admits that the CBI includes several sensitive non-GSP horticultural items: tomatoes, cucumbers, squash and eggplant, but feels that opening up U.S. markets to these markets will have a minimum effect. Statement of Richard A. Smith, Administrator, Foreign Agricultural Service, United States Department of Agriculture, before the Committee on Ways and Means, Subcommittee on Trade, March 17, 1982, p. 5. We wonder why these items were determined to be sensitive in the first place; and, if these commodities have so little impact at this time, we question the necessity of completely revising the Trade Act of 1974 and the wisdom of abandoning the procedures for GSP petition which Congress determined were necessary before duty-free treatment is granted.

We suggest that nothing has been presented in the CBI as to why the Caribbean Basin countries cannot petition for duty-free treatment under the GSP petition procedures. Congress intended that such procedures be followed. The procedures provide an opportunity for all parties to comment on the petition; and, the impact of granting the petition on the domestic industry is considered. This is fair, as Congress intended, and as it should be. The CBI changes all of this.

In our opinion, a decision granting duty-free treatment for all products coming from the Caribbean Basin runs contrary to the letter and spirit of the 1974 Trade Act and its implementing regulations and, quite simply, is unnecessary at this time.

In summary, after due deliberation and comment, Congress has legislated the procedure for adding new products to the Generalized System of Preferences. There are sound reasons for these procedures and we are not persuaded by the CBI that they should be abandoned as proposed. For example, if the CBI is passed in its present form, there will be no information as to how GSP treatment of the requested article would affect the petitioners' business and the industry producing like or directly competitive articles in the United States. In addition, other salient information as to production capacity, employment, prices and sales and how these factors might change with and without GSP treatment of the product will be unavailable. Such basic economic data should be the basis for determining whether or not to grant GSP treatment. The proposed CBI simply does away with any economic justification for duty-free treatment.

FLORIDA TOMATO INDUSTRY

The Florida Tomato Industry at one time provided nearly all the tomatoes consumed in the United States during the winter months. A large part of this market, however, was lost due to imports from Cuba. Now, Mexican imports seriously jeopardize the Florida Tomato Industry. We expect that Mexico will continue to ship tons of tomatoes to the United States on consignment or at prices which clearly are below their cost of production. We suspect this is happening right now.

Given this highly competitive and economically fragile and sensitive environment, the entry of tomatoes (and other sensitive agricultural products) from the Caribbean countries most certainly would be economically destructive to the Florida agricultural industry. Further, to permit duty-free status for all perishable agricultural commodities from the Caribbean Basin countries without any justification or any requirement for reciprocity creates, in our opinion, a dangerous precedent which could result in even further economic advantage being granted to countries such as Mexico.

CBI's Remedy for Injury to Domestic Industry

With regard to perishable products the CBI proposes that a petition alleging injury from imports from beneficiary companies be filed with the International Trade Commission and the Secretary of Agriculture with a request that emergency relief be granted with respect to such products. Within fourteen days after filing the petition, the Secretary of Agriculture can then determine whether importation of the perishable product is a substantial cause of serious injury, or threat thereof, to the domestic industry involved and that emergency action is warranted. If he so determines, he then advises the President. The President, then has seven days to issue a proclamation withdrawing the duty-free treatment provided or publish a notice of his determination not to take emergency action.

Such a remedy is unworkable and unrealistic as it pertains to perishable commodities. Moreover, the procedures contain inadequate and indefinite standards for review and are susceptible to subjective and therefore arbitrary considerations.

Parenthetically, we question the efficacy in any case of filing a petition under the Antidumping Act for perishable commodities. We note that members of the Florida vegetable industry filed such a petition with respect to imports from Mexico over four years ago and that the matter is still unresolved. Such relief is really no relief at all. The CBI proposal, even with its emergency provision, in our opinion, does not adequately address the issues involved.

The Administration posits that the foregoing remedy will result in speedy action on harmful surges of perishable agricultural products. We disagree. Moreover, Ambassador Brock believes that the CBI does not impose the threat of injury to any affected U.S. industry. Again, we disagree. Ambassador Brock supplied no economic data for this statement and it appears that he is down-playing the history of the GSP petition process since there are a number of products which have been eliminated through the GSP petition process or by the competitive needs limitation. If certain products (such as tomatoes) have been determined to be sensitive and therefore a duty imposed, we wonder why without any supporting documentation the same products are no longer sensitive and no longer adversely impact on U.S. industry.

If the CBI initiative is passed by Congress, the Exchange requests that some type of limitation be placed on perishable agricultural imports from the Caribbean Basin countries. Not only is this fair to domestic agricultural industries since the Caribbean Basin countries' products compete directly with Florida agriculture, but also it is fair (and reciprocal) because the Caribbean Basin countries have imposed stiff tariffs on agricultural products from the United States. For example, Jamaica imposes a tariff on tomatoes imported into that country of 53.85 cents per 100 kilograms of fresh or chilled tomatoes and a 25% tariff on all preserved tomatoes.

In addition, we note that the burden of the CBI is to be shared by other donor countries including Mexico. We recommend that steps be taken to assure that Mexico provides the same duty-free treatment to the Caribbean countries as the United States. Mexico's contributions to the CBI of concessions and supplies of oil serve not only the Caribbean countries but itself. The Exchange suggests that duty-free treatment by Mexico will provide additional strong incentives to the economic development of the entire area and provide additional stimulus for free trade. In sum, we suggest that Mexico assist in assuring the burden of duty-free treatment -- the most important part of the Caribbean Basin Initiative -- be shared by all the donor countries. We suspect, however, that Mexico will not grant such duty-free treatment because, unlike the U.S., its trade policy protects its producers.

Alternatively, we suggest that "countervailing" appropriations or tax relief be "earmarked" for domestic producers of goods which compete directly with goods from the Caribbean Basin countries. Since the CBI is intended to provide preferential treatment to the Caribbean Basin countries so that these countries can gain entry into the U.S. market, it seems only fair that compensating benefits be given to the domestic producers of competing products whose markets have been singled out to be taken over by imports from CBI beneficiary countries.

At the head of the list are perishable agricultural products -- the majority of which come from Florida. Once again, it appears that U.S. policy is to sacrifice the Florida perishable agricultural industry in the hopes that some stability and progress will occur in the Caribbean region. One thing is certain, though, if the program works as proposed, Caribbean countries' imports into the United States will benefit at the expense of Florida producers. Florida presently is suffering from the results of such a policy with Mexico.

OTHER PROBLEMS REGARDING THE CBI

The CBI overlooks or fails to deal adequately with a number of issues involving Florida agriculture. For example, the representatives from the U.S. Customs Service indicated that Customs does not have adequate manpower to perform its function of export control. Customs, accordingly, intends to employ a "GSP type of control" which involves accepting the manufacturer's declaration of origin and value without independent verification. While acknowledging that origin rules are necessary to prevent transshipment of merchandise from ineligible countries through Caribbean beneficiary countries, the Customs Service recognizes there will be substantial problems in enforcing this rule and that they will have difficulty determining if products are grown or produced by beneficiary countries.

The Customs Service proposes "documentary controls" to monitor and enforce the origin and value criteria in the CBI legislation. The Exchange believes that the proposed "documentary controls" will not adequately address the problem. Such controls are ineffective and *post facto* thereby permitting the potential for serious damage to domestic industries. In addition, the Customs Service has not assessed the scope of this problem or the impact on domestic industry. Certainly, this information must be developed prior to the enactment of any legislation. Otherwise, the CBI presents an opportunity for transshipment with admittedly little possibility that the transshippers will be caught. Moreover, the damage to domestic industries will have occurred and, in this scheme of the CBI, it is possible that the beneficiary countries will not have derived any benefit from such transshipments. In summary, if Customs is to enforce the law, it must do so in a manner that will ensure the integrity of the CBI. The proposed documentary controls simply do not measure up.

In addition, the Exchange believes that it is necessary for all perishable agricultural products and/or their containers coming from the Carribean Basin countries to be labeled as to their country of origin so that U.S. consumers are aware of the origin of the product.

The Subcommittee should also develop specific economic trade data to assess the economic situation in each Caribbean Basin country affected as well as the same information for the U.S. industries affected or threatened and the estimate of the CBI's impact on each and the reasons therefor.

The CBI legislation states that in designating beneficiary countries the President will take into account inter alia countries' overall trade policies including the use of export subsidies and export performance requirements. Such an analysis should include full details of the affected Caribbean Basin countries' own tariff and non-tariff barriers to entry and export subsidies. The Exchange believes that the trade barriers erected by many of the Caribbean Basin countries are as restrictive as Mexico's with regard to perishable agricultural commodities and should be considered before any permanent action is taken by Congress.

The Chairman of the International Trade Commission testified that likely injury petitions could be in the area of perishable agricultural products. No other industry or products were so mentioned. Further, Chairman Alberger indicates "...there may be some uncertainty generally as to the causation standard for analysis of the impact of imports from the Caribbean Basin." And, Commissioner Alberger notes that the CBI legislation does not now require advice from the International Trade Commission on the probable economic effect on domestic industries of removing current duties on products from prospective CBI beneficiaries and that "...at least for the past few decades, the Congress has not delegated tariff reduction authority to the President without requiring such advice." The foregoing indicates not only a need to amend the legislation at least to address ITC's concerns but also indicates the importance of determining the probable economic effects of the CBI on domestic industries.

Other than conclusory statement that the CBI does not impose the threat of injury to any affected industry (Ambassador Brock's statement, p. 5), no substantive economic data on this issue has been supplied by the Administration. It is significant to note that in the face of the numerous meetings, task forces, discussions and the like which formed the genesis of the CBI, the Congressionally-mandated Technical Advisory Committee to the U.S. Trade Representative was not convened once to provide its input on the CBI. As the Committee knows, Congress specifically provided for this Advisory Committee to provide domestic industries' input to the U.S. Trade Representative on all significant trade issues.

The Exchange believes this is a significant trade issue and has the potential to harm significantly the Florida Tomato Industry. The Exchange believes the Fruit and Vegetable Subcommittee would have advised Ambassador Brock that the CBI as it pertains to perishable agricultural commodities could greatly harm U.S. industries and, as written, does not offer adequate safeguards to protect the domestic perishable agricultural industry. Given the potential for harm to domestic perishable agricultural industries, and the fact that a Congressionally-mandated mechanism is presently in existence to put additional products on the GSP list, the Exchange believes that the CBI at a minimum should exclude duty-free treatment for perishable agricultural products, which the Administration admits are sensitive and, therefore, compete directly with U.S. producers.

The CBI legislation requests duty-free treatment for all products for a 12 year period. Justification for this statement is weak at best. Given the fact that trade with the CBI countries is not reciprocal and that a case has not been made to extend duty-free treatment to sensitive perishable agricultural commodities, the 12 year period should be deleted and, if any change is made, it should be a yearly figure with Congressional oversight of the program.

In addition, it is significant to note that some Caribbean countries are not pest-free. Recent problems in California and Florida regarding the Mediterranean fruit fly indicate the real and present danger of pests entering into the United States from countries which have pest problems. Some Caribbean countries have problems with the Caribbean, Mexican and Mediterranean fruit flies as well as the citrus canker. The CBI attempts to deal with this problem with promises of educational advice, and technical assistance; however, this is not enough and an outbreak of a fruit fly or some other foreign pest infestation literally could cost the State of Florida as much money as the President is requesting for additional assistance to the Caribbean countries. The Committee must not allow the CBI to go forward without adequately dealing from an enforcement point of view with this most serious problem.

SUMMARY AND CONCLUSION

There is a great need for United States foreign trade policy to be both reasonable and fair. It should protect the jobs of Americans whose source of livelihood is removed or threatened by foreign competition. For many years the U.S. government has adopted the philosophy of inviting progressively greater volumes of assorted commodities to be marketed in the United States, irrespective of their effect on U.S. producers, the Nation's employment situation, and the Nation's balance-of-payment position. As a consequence, steadily increasing imports such as those from Mexico have forced a number of domestic producers out of business, taking a steady toll of jobs across the country. The Exchange believes that we should be striving for truly reciprocal trade with the proper restraints necessary to prevent serious economic injury to our own industry, as other nations have done for many years in the past and are doing today.

The CBI continues this unfortunate trend. The Exchange recognizes this decision is political and takes into account many factors. However, a mechanism is in place that would permit expansion of duty free treatment for Caribbean products, if justified.

Since the United States takes nearly three-fifths of the Caribbean region's exports, with over 80% of them duty free and provides a major portion of these countries' income by our tourists, we question the necessity and urgency of placing all commodities under GSP given the cited harm to domestic producers and lack of any appropriate justification for taking such an action.

As mentioned above, the Exchange believes the CBI is contrary to both the letter and spirit of the Trade Act of 1974 and the Tariff Act of 1930. Granting GSP status across-the-board on perishable commodities surely will aggrevate an already difficult situation for Florida and U.S. producers and workers.

We suggest that Mexico as partner-donor with the United States and a major beneficiary of preferential treatment on perishable agricultural commodities from the United States, grant the same or similar treatment to imports from the Caribbean Basin countries.

The Exchange understands the problems that exist in the Caribbean Basin region and the need to provide support to the Caribbean Basin countries to help them help themselves. However, the Exchange is not willing to be fodder in this fight. The CBI, as it pertains to tomatoes and other competitive-sensitive products should not be enacted. No case has been made for the proposition that granting duty-free treatment to perishable agricultural commodities will assist the Caribbean Basin countries. On the contrary, adopting the CBI has the potential to cause serious problems for Florida tomato growers, other Florida and U.S. producers and labor.

The intention to help our neighbors is laudatory and we support proposed efforts to increase technological and scientific help, provide additional food assistance and assistance on P.L. 480 projects, assistance to improve animal, plant, health, and inspection services, and expand agricultural research and training assistance. However, the Exchange believes strongly that duty-free treatment for perishable agricultural products is not warranted and will cause harm to the Exchange's members, other U.S. producers and labor.

Given the foregoing, the Exchange respectfully requests that the CBI legislation be amended to exclude duty-free treatment of perishable agricultural commodities. In addition, the Exchange requests that the concerns raised above be addressed substantively before any action is taken on this legislation.

Mr. Chairman The Exchange stands ready to assist you and the Committee in any way that we can. We are hopeful that the comments made herein together with those of other concerned and affected associations, industries, and individuals, will assist the Committee in its efforts to deal with rendering assistance to our neighbors in the Caribbean Basin area in a responsive fashion while at the same time protecting the interests of those affected in the United States.

SANTURCE, PUERTO RICO, *March 17, 1982.*

Chairman, Ways and Means Committee,
U.S. House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN. I thank you for taking the trouble of shaping the Caribbean Basin Project based on President Reagan's proposals largely inspired by imminent arrival of Russian engineers and soldiers in Central America and by the real probability of the spreading of communist guerrillas into Mexico from Cuba, Nicaragua and El Salvador via Guatemala.

My appraisal of the situation is that thousands of Russian tanks may be now ready at Russian ports of embarkation for shipment to Nicaragua and I feel the concern of President Reagan, of Mr. Alexander Haig and of Mr. Caspar Weinberger is well founded. The United States is now facing a critical thrust against its integrity as a nation and republic by way of Cuba and Nicaragua.

The Caribbean Basin Plan is good but is not enough to halt the communist thrust against the United States via Mexico and Cuba. It is my honest belief that the United States must take swift military action to neutralize Cuba, Nicaragua and to protect El Salvador, Guatemala and Mexico too. We cannot deter the Communist aggression in the Western Hemisphere except by swift military action. Any other palliative measure will only play into the hands of Fidel Castro and Breshnev.

We must act swiftly in order to prevent the proclamation of a Soviet Republic in Nicaragua, El Salvador and Guatemala. And we must invoke the Monroe Doctrine and the Manifest Destiny of the United States otherwise we are headed for real trouble: the disintegration of United States security and the fall of democracy to the Communist Imperialists.

In connection with Puerto Rico the communists are also quite active. As you know Puerto Rico is a U.S. Commonwealth, an integral part of the United States body politic. Puerto Rico is a municipal segment of the United States still under the territorial clause of the United States Constitution. We are a domestic area of the United States. In 1953 I talked in person to Mr. Ralph Bunche the Secretary General of the United Nations at El San Juan Hotel at which time he said: "The grant and approval of the Commonwealth Constitution never changed the territorial or constitutional ties of Puerto Rico towards the United States for such grant was merely a grant of self-government in local matters only while the United States reserved all the rights belonging to the U.S. Federal Branch of Government". That was precisely Congressional intent in giving consent and approval to Public Law 600 that authorized the Commonwealth Constitution for Puerto Rico. And that was the will of the Puerto Rican voters (American citizens) like me who voted for the Puerto Rico-U.S. Commonwealth Constitution. At that time Senator O'Mahoney said "With the passing of the Commonwealth Constitution the rights, privileges and immunities of American citizens will be respected as if Puerto Rico were a state of the Union. U.S. federal authority shall never be impaired thru any legislation passed by the Puerto Rican Legislature. Any future amendments must be consistent with the Constitution of the United States, the Federal Relations Act and Public Law 600 which grants this Constitution". The sovereignty of the U.S. and U.S. interests were duly protected, so was the Treaty of Paris of 1898 that transferred Spanish sovereignty to the United States of America and therefore the right of the American citizens of Puerto Rico to seek statehood and the blessings of equality and freedom were also protected. As United States citizens the only goal compatible with our citizenship is full fledged statehood under the spirit and written word of the Constitution of the United States. The United States has kept Puerto Rico as a very dear U.S. Territory since the year 1898 and the history of our country and the U.S. tradition reflects that the United States has only kept territory that strengthens our country. That is why since 1898 and thru Congressional legislation, regulations, Presidential Proclamations and court decisions and interpretations the will and the spirit of the United States has gradually been extended to the people of Puerto Rico. The vested rights of the 3 million American citizens of Puerto Rico are sacred and our constitutional ties with the United States are all one and the same.

Under such circumstances we cannot grant Puerto Rico any measures that are different from those governing the 50 States of the Union. We cannot grant Puerto Rico special deals that are denied the 50 states.

Yes, Mr. Chairman, the communists and other enemies of statehood are always looking for these special grants that would split Puerto Rico away from the United States Constitutional system.

That is why I raise my strongest objections against the special grants of tariffs, immigration, shipping laws, customs, and what not which obviously constitute an attempt to break not only with the uniformity clause of the Constitution in dealing with states and with territories but also to break in the long run with the Constitution of the United States, the Treaty of Paris and United States sovereignty and authority over a domestic part of our nation.

I do hereby recommend that in dealing with the Caribbean and South American nations, also Canada in trade and business we should be prepared to allow credit payments to exceed 90 days and to become 6 months plus six additional months and if necessary allow more time so as to give a push to flourishing business relationships that in time shall strengthen our political ties.

Create a special Bank for Development for these peoples at low interests in such a fashion that loans could be granted to their government per se but also to big as well as small businesses, directly to them.

Lower air travel fares between the Hemispheric nations and the United States and promote the creation of passenger ship lines with low fares for a better cultural interchange with these countries.

Grant tax exemptions for the establishment of foreign capital factories in the United States and get reciprocal treatment to U.S. corporations in those countries.

And finally grant statehood to Puerto Rico now for we need a total identification with the United States Constitution. The business world at the mainland United States need constitutional assurances to invest in Puerto Rico with the grant of Statehood. Tourism needs Statehood to flourish. That sense of equality and decency calls for immediate statehood. The Congress should approve a joint resolution to order a referendum to vote yes or no for statehood in Puerto Rico. Congress has the authority under the territorial clause so as to prevent the communist activists decide the status problem of Puerto Rico and to avoid further embarassment at the United Nations. The people of Puerto Rico themselves are tired of being pushed around. Give them a decent, democratic deal, now.

Some Puerto Rican athletes are ready to participate in Pan American Games in Cuba on August this year. Do you think this is right at the time Cuba is exporting revolution and provoking bloodshed among their latin brothers in Central America? It is not right!

Respectfully,

HARDING FRANCO-SOTO.

STATEMENT OF BURTON A. LANDY, PRESIDENT, AND THOMAS G. TRAVIS, COUNSEL, INTERNATIONAL CENTER OF FLORIDA, INC.

SUMMARY

This statement is being filed by Burton A. Landy, Esq., Peninsula Federal Building, 12th Floor, 200 S.E. 1st Street, Miami, Florida, (telephone—(305) 358-9300), as President of the International Center of Florida, Inc. and by Thomas G. Travis, Esq., Sandler & Travis, P.A., 444 Brickell Avenue, Suite 500, Miami, Florida 33131 (telephone—(305) 358-4213), as Counsel to the International Center of Florida, Inc.

The statement is submitted on behalf of the International Center of Florida, Inc. The International Center highly commends the general structure and principles of the Caribbean Basin Initiative. The International Center favors liberalization of the one-way free trade zone concept. Suggested modifications include reduction of Caribbean input requirements to fifteen (15) percent and allowance for the value of United States materials and relevant costs. The tax package and the amount of direct financial assistance should be increased to encourage investment and initiate immediate recovery. The Center agrees that foreign bank secrecy laws should be eliminated or relaxed to promote effective law enforcement in tax as well as international trade transactions.

STATEMENT

This statement is filed on behalf of the International Center of Florida in response to President Reagan's announcement of the Caribbean Basin Initiative. The International Center of Florida is a group of businesses and organizations in Miami, Florida dedicated to the development and expansion of international activities, with a particular concern for matters of international trade.

The International Center highly commends the general structure and principles of the Caribbean Basin Initiative (CBI). The severe economic crisis in the Caribbean region poses a serious threat to the political and social stability of the Basin, and to the security of the United States. The CBI represents a major step toward correcting these deteriorating conditions. It is apparent that the developed countries must take certain action to arrest the economic crisis and promote recovery in the Caribbean Basin.

The structure of the CBI is crucial to accomplishing the basic objectives of the program. Since the utimate goal looks toward a viable economic framework through private sector development, assistance from the United States must lay a solid foundation for extensive entrepreneurial activity. Accordingly, all elements of the plan should be executed in the manner that will most successfully achieve adequate living conditions, a level of self-sufficiency, and stable political institutions.

The legislation proposes a program based upon three (3) major economic measures. The focus of the program is the one-way free trade zone concept. This measure represents a significant move in the right direction to lower the standards for establishing country of origin to qualify for duty-free treatment of products imported from the Free Trade Area.

Although similar in nature to the Generalized System of Preferences, the CBI includes different requirements for eligibility. Under the Generalized System of Preferences, the value of materials and direct labor from the beneficiary country included in the subject article must equal or exceed thrity-five (35) percent of the appraised value of the imported goods. The CBI proposal would reduce this percentage to twenty-five (25) percent, and would further liberalize the requirements by permitting the costs of services to be applied toward the twenty-five (25) percent and by allowing inclusion of the relevant costs incurred in any of the Caribbean region countries.

In our opinion and experience, the country of origin requirements should be relaxed even further. Experience under the Generalized System of Preferences has established that the United States Customs Services will interpret "direct costs of processing" in an exceptionally narrow manner. Management and overhead costs, regardless of significance, relevance, and necessity to operations in the CBI country, will not be includable in the calculation. High technology and costs of materials and components, most of which are currently not produced in any CBI country, will prevent the inexpensive "direct cost of processing" from reaching the twenty-five (25) percent standard.

Based upon the foregoing analysis, we recommend the following modifications of the legislation:

(i) The twenty-five (25) percent requirement should be lowered to fifteen (15) percent. This amount reflects a more realistic level of value which might be added by existing or incipient industries in the beneficiary countries.

(ii) The cost or value of any United States material, components or labor should be included in the twenty-five (25) percent requirement. This change would encourage development of industry in the United States, would provide an advantage to this country over other industrialized countries looking to the Caribbean market place, and is consistent with the provisions of the CBI proposal regarding value added by Puerto Rico and the Virgin Islands.

The second major element of the program is the availability of a tax credit for investment in qualifying Caribbean Basin countries. Although the tax incentives have been criticized on the grounds that they will discourage investment in the United States, we believe that a positive incentive to investors is an exceptionally important factor necessary to the success of the CBI program.

We believe that the tax package should be increased in order to entice United States investors into these areas with historically unstable political and economic conditions. The incentives must overcome any hesitation to invest in undeveloped markets with insufficient resouces and personnel. Many private groups, including the Council of the Americas, have presented various possible tax incentives to the Office of the Special Trade Representative. We urge that this Committee and the Administration review these suggestions for possible amendment of the current CBI proposal.

Thirdly, it is our opinion that the amount of direct financial assistance is too small in light of the critical conditions in the recipient countries. Immediate monetary aid is necessary to commerce correction of extensive structural problems, inflation, and scarcity of trained personnel. In order to fulfill the proposes of the program, the Administration must be authorized to insure that monies are well targeted in the CBI economies.

We agree with the provisions directed toward elimination of bank secrecy laws which impede law enforcement activities in the United States. However, we believe that the secrecy laws should be relaxed with respect to other areas of investigation. The bank secrecy laws have also prevented United States authorizes from investigating traditional frauds in connection with international trade activities. For example, one United States importer paid in excess of $500,000 for goods which did not exist. The seller obtained payment based upon forged documents, evidencing a sale and shipment of the goods. The monies paid by the United States importer were traced by the FBI to a bank protected by the Bahamas Bank Privacy Act and, thereafter, the investigation went no further. This type of criminal activity should not be protected by offshore banking laws. The CBI legislation could authorize efforts in this area by amending Section 303 to include official investigations into criminal activities.

Announcement of the Caribbean Basin Initiative demonstrates the seriousness of the problems facing the Caribbean region. The basic structure of the program can be quite effective in combating this economic crisis and establishing a framework for continuous development. The key, however, is to administer the proposals in the manner that will most effectively realize the President's objective in light of the limited capabilities of the people.

Most importantly, the one-way free trade zone concept must be implemented to create a solid framework for economic development. Accordingly, input requirement for the trade program must be relaxed in order for these people to take advantage of United States assistance. The direct financial assistance must be properly allocated to solve emergency problems and stimulate growth. The investment incentives must be of sufficient magnitude to outweigh the substantial risks involved in developing new markets with crude and inadequate resources. Self-development remains critical to recovery and stability of the Caribbean Basin. The Administration must coordinate all measures of the CBI program to allow the people in the Basin to achieve economic progress and an adequate standard of living.

The International Center of Florida appreciates the opportunity to comment on the Caribbean Basin Initiative.

JAMES L. NELLIGAN
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Congress of the United States
House of Representatives
Washington, D.C. 20515

ARMED SERVICES COMMITTEE
SUBCOMMITTEES:
READINESS
INVESTIGATIONS

EXECUTIVE COMMITTEE OF THE
REPUBLICAN STUDY COMMITTEE

NORTHEAST-MIDWEST
CONGRESSIONAL COALITION

TASK FORCE ON ENERGY
CHAIRMAN, COAL SUBCOMMITTEE

TASK FORCE ON HEALTH AND
ENVIRONMENT

TOURISM CAUCUS
STEEL CAUCUS
WOOD CAUCUS
TEXTILE CAUCUS

March 30, 1982

The Honorable Sam M. Gibbons
Chairman
Subcommittee on Trade
House Ways and Means Committee
233 Cannon House Office Building
Washington, D.C. 20515

Dear Sam:

The purpose of this letter is to comment on the proposed Caribbean Basin Initiative, which has been the subject of recent hearings in your subcommittee. While I support the basic objective of the initiative, which is to promote the economic revitalization of the region, I have major reservations about one important aspect of it.

I do not believe that the initiative, as it is presently structured, affords enough protections for the American shoe industry. The initiative calls for elimination of all duties on imports from the Basin except textiles and apparel items. While I applaud the exclusion of these items, I feel that similar exclusions should be provided for shoes and footwear.

Existing levels of import penetration are already crippling the American shoe and footwear industry. Imported shoes now account for almost half of the American domestic market. Failure to exempt shoes from the duty-free provisions of the Caribbean Basin Initiative will result in greater market penetration by imports, and further loss of jobs for American workers. I therefore urge your subcommittee to take appropriate actions to ensure that shoes and footwear are provided exemptions similar to those afforded textiles and apparel.

I request that you make these comments a part of the written record of your subcommittee's hearings. I will be happy to offer any assistance I can toward amending the initiative to provide protections for our shoe industry.

Sincerely,

James L. Nelligan

James L. Nelligan
Member of Congress

JLN:mb

OXBOW CONSTRUCTION CORP.
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March 15, 1982

The Honorable Sam M. Gibbons,
Chairman
Subcommittee on Trade of the
House Ways and Means Committee
House of Representatives
Washington, D. C. 20510

My dear Congressman Gibbons:

It has come to my attention that hearings are to be held during the middle of March to receive testimony on the Caribbean Basin Initiative, with particular emphasis on the proposed trade and tax concessions.

I would like to take this opportunity to put in a word for the Dominican Republic. I am an American citizen and I have worked and lived in the Dominican Republic for varying periods since 1949. Before that time, my father lived there for many years. So I do feel that I have a good knowledge of the country and its people. We are in the road construction business and have worked during those same years in Nicaragua, Guatemala, El Salvador, Honduras, Panama, Venezuela and the Guianas. Our main interest, however, has always been in the Dominican Republic.

It has always been distressing to me that the interest of the United States in this area has only been aroused after a fire was started and in full blaze, which now seems to be the case in Central America. In 1965, the Dominican Republic received our full attention when it was a thought that a Communist takeover was imminent.

The Dominican Republic is the most populated island in the Caribbean chain. I believe it is the only island in the Caribbean (along with Haiti) not to have an affiliation and preferential treatment from either their present or former colonizers. The entire Bahama chain has its preferences with Great Britain as do many of the islands in the Lesser Antilles. Jamaica also has its affiliation with Great Britain and receives preferential treatment. The other islands have been associated by colonization with either France or The Netherlands and have received preferential treatment from them. Cuba has its affiliation with Russia and receives preferential treatment from them. Puerto Rico has its tie with the United States with its obvious advantages.

However, when one looks at the assistance to the Caribbean Basin, the actual 1980 and 1981 assistance is going down. The current 1982 budget and the 1982 Congressional presentation show a slight trend up from 1981 but still down from 1980.

In 1983, the projected aid to the Dominican Republic will be approximately $47 million, with a population of over 5½ million. Jamaica has a population of slightly over 2 million and will receive in excess of $112 million. Jamaica, as well as the other islands in the area (other than the Dominican Republic and Haiti) also received preferential treatment from the European community by way of their affiliations with Great Britain, France and The Netherlands.

If one looks at a map of the Caribbean area, most shipping must pass to the north or south of the Dominican Republic to get to Central America and to the Panama Canal. If one wanted to have bad dreams, a look at this map and the possible expansion of a Russian-Cuban influence to the island of Hispaniola (Haiti and the Dominican Republic) would turn the bad dreams into a nightmare.

At present, the Dominican Republic is a friend of the United States. The United States should help its friend in a substantial way while it can in a calm, orderly and rational fashion, rather than to wait for trouble to strike and then have to pour in huge amounts of money to bolster a neglected situation. Example: El Salvador with a population of 4½ million, with a projected 1982 assistance budget of $104 million and a 1983 budget of $164 million.

A very close look should be taken at the strategic location of the Dominican Republic and its crucial importance to the rest of the Caribbean Basin as well as to the United States.

Thank you for bearing with my comments.

Very truly yours,

OXBOW CONSTRUCTION CORP.

James J. Hagan

James J. Hagan
President

JJH:b

STATEMENT OF LAWRENCE A. KIRKHAM, CORPORATE CUSTOMS MANAGER, SYNTEX CORP., PALO ALTO, CALIF.

Syntex Corporation respectfully wishes to file comment upon the Caribbean Basin Economic Recovery Act (herein referred to as the "Act") which was recently submitted to the Congress of the United States of America.

Syntex Corporation is dedicated to research in the life sciences. Our human health and life science products include pharmaceuticals; veterinary drugs; animal health products; dental instruments, equipment and models; diagnostic assay systems; beauty care products; fine chemicals; and ophthalmic products. Syntex' diverse international activities presently include manufacturing facilities in the Caribbean Basin.

While Syntex Corporation is fully supportive of the objectives of the Act, we submit that the proposed Rules of Origin preclude the free trade of research intensive products.

To elaborate, a definition of the typical "research intensive product" is vital to the understanding of this submission. Research intensive products normally entail a disportionate level of research and development costs the recovery of which is inherent in their market value. This fact does not preclude their duty-free treatment under the Canadian, European Economic

Community, or European Free Trade Association Generalized System of Preferences (GSP) Rules of Origin; however, such goods are generally inelligible for duty preference into the U.S. as a result of the U.S. Rules of Origin. To illustrate this statement, we can offer the following examples of the application of other countries' Rules of Origin to a pharmaceutical chemical:

Costs:	Imported Materials	$100
	Local Labor & Overhead	$200
	Local Materials	0
	Total Cost	$300
	Value	$1,000

Canadian GSP: Foreign content (ie. Imported materials; Canadian materials, if any, are included as local origin) cannot exceed 40% of assessed value; therefore, $100/$1000 = 10%: Goods qualify.

EEC Lomé II: Foreign content (ie. Imported materials; EEC materials, if any, are included as local origin) cannot exceed 20% of assessed value; therefore, $100/$1000 = 10%: Goods qualify.

U.S. GSP: Originating content (ie. Local labor, overheads, and materials) must be equal or greater than 35% of assessed value; therefore, $200/$1000 = 20%: Goods disqualified.

U.S. CBERA: Originating content must be equal to or greater than 25%: Goods remain disqualified.

The foregoing illustrates the inequity of applying the U.S. added value criterion to research intensive products. Clearly, in this example the imported materials costing $100 per unit have been transformed by the manufacturing or processing operation conducted in the beneficiary country into a product valued at $1000 per unit. By any reasonable test of added value, such activity should qualify for free trade.

Syntex, therefore, does not believe that the objectives or intent of the Act can be achieved without a revision of the Rules of Origin. We recognize that safeguards are required to preclude "pass through" operations from qualifying, but believe that this can be achieved by adopting the effective methodology employed by the EEC to exclude "minimal processing" operations as defined in their Rules of Origin.

We would like to submit for consideration three alternative approaches to forming the U.S. Rules of Origin:

(i) To adopt the Canadian approach under GSP which stipulates that the cost of materials imported into the beneficiary country cannot exceed a stipulated percentage of the appraised value.

(ii) To require that costs of manufacture incurred in the beneficiary country be no less than a stipulated percentage of the total cost of manufacture.

(iii) To measure added value by subtracting the unit cost of materials imported into the beneficiary country from the appraised value of the exported item and to require that such added value be no less than a stipulated percentage.

In accordance with the apparent intent of the proposed Act and the limit specified therein, the stipulated percentages would be expressed as; (i) 75%, (ii) 25%, (iii) 25%.

Definition of locally incurred costs in all cases would include local materials, labor and production overhead, all in accordance with Generally Accepted Accounting Principles and consistant with CFR 19, Section 10.177, as amended.

In conclusion, we urge that review and modification of the Caribbean Basin Economic Recovery Act Rules of Origin be implemented with a view to qualifying research intensive products for free trade within the intent and spirit of the Act. The opportunities for free trade should extend to products from all business segments to encourage the establishment of a broad-base economy. With revised Rules of Origin, Syntex believes that the Act will provide an impetus for industry to invest in the Caribbean Basin.

STATEMENT OF HAROLD F. CARY, EXECUTIVE DIRECTOR, THE U.S. TUNA FOUNDATION, IN BEHALF OF THE TUNA INDUSTRY OF PUERTO RICO, AMERICAN SAMOA, CALIFORNIA, AND HAWAII

Governor Romero-Barcelo in his statement to the Subcommittee, which supported the Caribbean Basin Initiative, presented a section on tuna concluding with a request that, ". . . this Subcommittee—exclude processed tuna from the duty-free treatment of the Caribbean Basin Initiative."

There is impressive array of factual data which support this request.

Puerto Rico tuna processing plants produce 40 percent of United States canned tuna production (based on the record of the past several years). It is the second largest tuna processing center in the world. The island areas of Pureto Rico, American Samoa and Hawaii represent about 55 percent of U.S. production with the continental United States producing 45 percent. California is the largest producing area.

There are five tuna processing plants in Puerto Rico representing many millions of dollars of investment and, particularly, replacement value. Three are located in Mayaguez—two in Ponce, both areas of high unemployment.

These plants employ annually or seasonally about 6,000 persons. The governor's presentation states that they represent from 4 to 5 percent of Puerto Rico's manufacturing employment. These employees both union and nonunion, operate under labor standards including wages and hours regulations which are counterparts of United States laws adjusted for regional differences.

The value of canned tuna production in 1980 and 1981 has averaged $440 million.

Shipments of canned tuna (Schedule B number 1122500) plus by-products such as pet foods and fish meal and oil represent about 7 percent of shipments from Puerto Rico to the United States. Canned fish Schedule B number 1122500 is the largest single line item in the Bureau of the Census reports (FT800).

Puerto Rico's tuna installations were a prime factor in providing an outlet for the catches of the developing tuna fisheries of many nations fishing the Atlantic Ocean. In 1981 Puerto Rico processors utilized about 30 percent of the total of tuna catches of the many nations, including developing nations, fishing the Atlantic.

United States tariffs on canned tuna have been reexamined in recent years. Following hearings in 1980, a decision was made May 28, 1981 (Federal Register page 28784) to deny petitions for tariff reductions. Labor, environmental and other standards required to produce in Puerto Rico confer decisive advantage to competing nations in the area should tariffs be eliminated. The entire industry on shore and at sea, in the islands and on the mainland would be adversely affected.

We respectfully request that you examine the subject of the processed tuna industry in Puerto Rico and the effect thereon of duty elimination. Those who have testified have stated that the industry can only be maintained by retention of existing tariffs. We support that position and point out that a method for reviewing tariff rates already exists in the Generalized System of Preferences.

EMBAJADA DE PANAMA,
Washington, D.C., April 14, 1982.

Hon. SAM M. GIBBONS,
Chairman, Subcommittee on Trade, House Ways and Means Committee, U.S. Congress.

DEAR CONGRESSMAN GIBBONS: It is our pleasure to present a written statement prepared by the special delegation from the Government of the Republic of Panama in regards to the Caribbean Basin Economic Recovery Act and the sugar products.

We hope that this written statement will prove useful as a background for your consideration of the subject matters involved.

Accept the assurances of our highest consideration and esteem.

(POR JUAN JOSÉ AMADO III AMBASSADOR.)

COMMENTS OF THE REPUBLIC OF PANAMA ON THE SUGAR PROVISION OF THE CARIBBEAN BASIN INITIATIVE

The Republic of Panama wishes to explain some facts and points about its sugar industry. We feel this to be necessary in light of the bill presented to Congress by the Executive Branch of the United States Government and known as H.R. 5900, "Caribbean Basin Economic Recovery Act."

The sugar industry in Panama, which was developed by both the private and public sector, dates back to 1913. The country has six sugar refineries, four of which are State-owned while two are owned by private enterprise. National sugar production amounts to approximately 246,000 metric tons. Roughly 158,000 metric tons are exported each year, all to the United States market.

One of the reasons why our country has developed this kind of industry is that the refineries are an important source of public jobs and at the same time, slow down migration from the countryside to the cities, thus holding down the excessive increase in the numbers of people living near the Canal.

It has been encouraging to watch the number of the new small businessmen in the various sectors of this branch of the economy. At present, the livelihood of 20,000 workers and approximately 3,000 medium and small independent producers of sugar cane depends on the industry. The multiplier effect of this means that 100,000 people depend directly or indirectly on this branch of the economy.

In 1981, sugar exports represented 16 percent of Panama's total exports, and total sugar production was somewhat more than 7 percent of its gross domestic product.

This shows the importance of the sugar industry for Panama's economy. Four percent of the country's economically active population would be affected if productivity were to drop off or if normal operations in the sector were to be disrupted. Any such fall in production would directly injure the weak economy of the private producer and farmer, would cause a measurable amount of social tension, and would provoke an explosive political instability. This could have a serious effect on the firm social peace enjoyed today in our country by thousands of Panamanians and foreigners, and indisputably, would have a negative impact on our Government's ability to maintain the security of the Panama Canal. Our country is located in an area of great social upheaval, and our first responsibility, which we share with our friends, is to ensure that it remains as peaceful as it has been thus far.

Section 103(c) of the Caribbean Basin Economic Recovery Act directly benefits Panama, and it is our view that this does not injure any sector of the United States sugar industry. Despite any injury it may cause us, regardless of circumstances, and whether or not Congress passes this bill, Panama's sugar exports will go to the American market, as they have in the past, since for very particular reasons, the port facilities serving our sugar industry do not enable us to explore other markets.

Some have suggested that during debate on this bill in Congress, some amendment should be made to the part referring to the exemption of the duty on sugar, by a reimbursement. Panamá considers this to be an inefficient system, because it could give rise to serious friction.

As to the claim by some sectors of the American sugar industry that we could reduce the sale price of our product, we consider this to be absurd, because it would mean that our country would be giving away benefits we have made great sacrifices to achieve, while in fact, all we would be doing would be partially recoup our losses. In the past, Panamá has been a beneficiary of the Generalized System of Preferences, and has always made appropriate use of the exemptions it has received.

As to the idea that Panamá would increase its sugar production under the benefits of the CBI, we must state here that our country is not in a position to make investments that would cause our economy greater losses, nor is it our policy to do so. Prices on the international markets are at their lowest point since the end of the last decade, and all indications are that they will remain at those levels, or drop even further during the next eighteen months or two years, as the result of the unfair policy followed by the European Economic Community (EEC) in blatant violation of the General Agreement of Trade Tariff (GATT). Having said this, we have concluded that we shall maintain our production of sugar levels tailored to our installed capacity, the current investment value of which is approximately U.S. $750,000,000.

The cost of producing sugar in Panama is one and one half times as much as the current price on the international market. Added to this, we have costs of marketing, transportation, duties, taxes, handling, etc. Since we are a developing nation, we find ourselves having to import all the inputs that are needed for cane production and sugar manufacture, at an estimated cost of more than U.S. $16,000,000.

More than 90 percent of these imported inputs come to Panamá from the United States. We should like to add that because our currency is strong, Panamá pays its agro-industrial workers what are probably the best wages in the region.

As long as there are people in our area who go hungry and who share lives of economic uncertainty, we must find democratic means to wipe out those diseases and place a roof over their heads. We cannot talk of observance of human rights, while we fail to give our peoples—to use Jefferson's words—"the right to life, liberty and the pursuit of happiness."

For the Special Mission of the Government of the Republic of Panamá on the Sugar Question within the Caribbean Basin Initiative.

AQUILINO BOYD
DARIÉN AYALA
CARLOS ARIAS CH.

STATEMENT OF J. ROYAL PARKER, PRESIDENT, J. ROYAL PARKER ASSOCIATES, INC., CHERRY HILL, N.J.

I welcome this opportunity to submit a statement of my views on the provisions of H.R. 5900, the proposed Caribbean Basin Economic Recovery Act, that relate to protection of the interests of U.S. private investors in the region.

Specifically, I refer to Section 102(b)(2) of the legislation, which prohibits Presidential designation of a country as a beneficiary country if it has explicitly or in effect expropriated property owned 50 percent or more by U.S. investors without making or offering to negotiate compensation to them.

I fully support Section 102(b)(2) and am convinced that its inclusion in the legislation is vital to the success of the Caribbean Basin program. As my own difficult and costly investment experience in Costa Rica shows, however, Section 102(b)(2) will offer full and meaningful protection to U.S. private investors in the region only if the Committee enunciates a clear Congressional intent to free the familiar legislative language from the limiting interpretations placed on it in the past by the Executive Branch and by the courts.

By way of background, I am an engineer and industrialist who has been engaged in the development of private sector industry in developing countries for twenty years, through J. Royal Parker Associates, Inc., and predecessor companies. As an example, I was one of the founders, in 1963, of Costa Rica's only petroleum refinery, Refinadora Costarricense de Petroleo, S.A.

In 1977, J. Royal Parker Associates carried out a partially AID-financed contract, which it had won in open competition, to determine the basis for establishment of Costa Rica's first industrial free port zone. Early in 1978, my company entered into a contract with an agency of the Government of Costa Rica (JAPDEVA, The Atlantic Zone Port and Economic Development Authority) for the establishment of Centraport, S.A., a 50-50 mixed company whose task was the creation of industrial free port zones, beginning with the Port of Limon.

Centraport, S.A. was then formally established, its initial share capital paid, its officers designated, its initial board meetings held, and most importantly, its validity as an undertaking of the government reviewed and confirmed by the Auditor General of the Republic, an official comparable to the Comptroller General of the United States. There can thus be no question as to the good faith compliance of Centraport, S.A. with Costa Rican law.

The task of arranging finance for Centraport's operations and for developing the interest of foreign manufacturers and other users of the Limon Zone fell to my company. We identified some twenty-two international companies as seriously considering establishing themselves in the zone, and we brought major investment banking sources into the picture. These efforts entailed very substantial investments of time, money and professional reputation on the part of J. Royal Parker Associates.

Shortly after the inauguration in May 1978 of President Rodrigo Carazo, it became abundantly clear that our government partner, JAPDEVA, had decided to, or had received instructions to, disavow our joint undertaking. Abruptly and arbitrarily, corporate activities were suspended and my communications at all levels of government went unanswered. No definite explanation has ever been given for the government's change of attitude on this project which was so vital to private sector development in the country.

After three years of repeated but unsuccessful attempts through administrative means to obtain compensation for the damages caused by JAPDEVA's actions, both financial and in terms of my company's professional reputation, I was forced on April 16, 1981, for statute of limitations reasons, to initiate legal action in Costa Rican courts.

That legal action, I regret to say, has no early prospect of resolution, much less of an outcome that will provide effective compensation. Because of the State Department's insistence on exhaustion of local remedies, a "Catch 22" situation exists: an injured investor is forced to sue because his government will otherwise not become involved, but once he sues, his government uses the fact of the suit to continue to decline involvement, even if the suit may take years. No small or medium size U.S. investor has the resources to cope with such a situation.

To compound the problem, even if the exhaustion barrier is overcome, the limited reading the State Department and U.S. courts have given to the term "property" as it appears in Section 102(b)(2) and prior expropriation statutes precludes effective relief for investors with experiences like mine. Property has been defined to consist substantially of physical assets, to the exclusion of contractual and other valuable rights. The reference in Section 102(b)(2)(B) to repudiation of an existing contract or agreement may appear to recognize contractual rights, but in fact it still requires a seizure or other effect on property to come within the area of protection. Unless the Congress expresses itself as favoring a broader definition of property in the context of arbitrary action by foreign governments, the broad investor protection intended by Section 102(b)(2) will be illusory.

It is not the purpose of this statement to prevent the designation as a beneficiary country of Costa Rica, a country to whose development I have devoted a good part of my life, and whose record of treatment of foreign investors is generally good. I do wish, however, to see meaningful protections built into the legislation now before the Committee, which will serve both to encourage a reasonable settlement by one government in my own case and to set a standard that will help prevent situations similar to mine occurring with other governments in the future.

Although the Committee may wish to consider a more far-reaching approach, I believe the current legislative language could be made to serve the above objectives. These objectives could be achieved if the Committee's report were to make an adequate record of Congressional intent that the Exective Branch use the opportunity of beneficiary country designations to protect those whose arbitrarily injured interests in foreign countries did not take the specific form of tangible property and for whom the exhaustion of local remedies represents in itself a compounding of injury.

I urge the Committee to make such a declaration. The alternative would be the perpetuation of an injury to a U.S. citizen by a country that is at the same time enjoying benefits provided by all U.S. citizens, the sanctioning of a serious erosion in the rule of law in international business transactions, and ultimately the failure of the very goal of the Caribbean Basin initiative of fostering private sector development in the region.

CONGRESS OF THE UNITED STATES,
HOUSE OF REPRESENTATIVES,
Washington, D.C., March 17, 1982.

HON. SAM GIBBONS,
Chairman, Subcommittee on Trade, Committee on Ways and Means.

DEAR MR. CHAIRMAN: The Subcommittee is to be commended for its early scheduling of hearings on both the trade and tax proposals contained in the Administration's Caribbean Basin Initiative.

The Administration is to be particularly congratulated on proposing to deny new tax incentives and benefits for investments in Caribbean Basin countries which do not provide for the orderly, due process exchange of tax information. It would be unconscionable for us to extend tax benefits to Nations which are serving as tax haven countries, and who serve as "drops" for billions of dollars of narcotic trafficking, organized crime, and tax evader "profits." The Cayman Islands, in particular, is notorious for attracting this kind of deposit.

I believe that the same type of "anti-tax haven" provision should be included in the trade provisions of the Administration's bill. We should not extend special duty-free treatment to Basin nations who refuse to cooperate with our law enforcement authorities. I hope an amendment to this effect will be offered in either the Subcommittee or the full Committee.

As you know, I have been a long supporter of due process in the IRS examination of individual and corporate bank records and I have favored more rigorous controls over IRS summons power. But the type of bank secrecy (and the advertising of that secrecy) offered by some Caribbean nations goes far beyond the needs of legitimate taxpayers. It is an invitation to gangsters, drug dealers, and tax cheats. It should not be rewarded in any way—either through trade liberalization or new tax benefits.

Sincerely,

FORTNEY H. STARK
Member of Congress

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